ANFOR CORPORATION

CANFOR

ANNUAL STATUTORY REPORT

Report to Shareholders • Annual Information Form • Management's Discussion and Analysis of Financial Condition and Results of Operations • Financial Statements

1991

Management's Responsibility

The information and representations in this report were prepared by Canfor's management. The consolidated financial statements were prepared in conformity with accounting principles generally accepted in Canada and, where necessary, reflect management's best estimates and judgements. The financial information presented throughout this report is consistent with that contained in the consolidated financial statements.

Canfor maintains systems of internal accounting controls, policies and procedures to provide reasonable assurance as to the reliability of the financial records and the safeguarding of its assets. The Internal Audit Department performs independent reviews of the accounting records and related systems on an ongoing basis to verify adherence to the internal accounting controls, policies and procedures. The Internal Audit Department reports its findings and recommendations both to management and the Audit Committee.

The Audit Committee of the Board of Directors is comprised of directors who are not employees of the Company. The committee meets periodically throughout the year with management, the internal auditors and the external auditors to review their respective responsibilities and to discuss audit plans, the results of reviews of internal accounting controls, policies and procedures, and financial reporting matters. The external and internal auditors meet separately with the Audit Committee.

The consolidated financial statements have been reviewed by the Audit Committee which recommended their approval by the Board of Directors.

Shareholder Information

Annual meeting

The annual general meeting of the shareholders of the Company will be held at the Four Seasons Hotel, Arbutus Room, on Monday, April 27, 1992, at 11:30 a.m.

Transfer agent and registrar

The Royal Trust Company
Vancouver, Calgary, Regina, Winnipeg, Toronto, Montreal and Halifax

Shares listed

Toronto Stock Exchange
(common and preferred shares)
Vancouver Stock Exchange
(common shares only)
Symbol: CFP

1991 price range of common shares

High: $29¾ per share
Low: $19⅜ per share

Number of common shares outstanding

25,868,610 shares,
as at December 31, 1991

Weighted average number of common shares outstanding during 1991

24,257,010 shares

Investor contact

A.G. Armstrong
Senior Vice-President, Finance
(604) 661-5417

Corporate Information

Auditors

Price Waterhouse
Vancouver, B.C.

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Report to Shareholders

Canfor's Annual Statutory Report to its shareholders is based on legally required information, specifically the Company's audited financial statements and management's discussion and analysis of financial condition and results of operations, as required by securities regulatory authorities. The Company's annual information form as filed with those authorities across Canada is included as well.

Prior to its annual general meeting, the Company will again be distributing a publication entitled "Overview", which will contain photographs and describe the Company's operations in greater detail. The meeting will be held in Vancouver, British Columbia on Monday, April 27, 1992.

1991 was the worst financial year in Canfor's history with a net loss of $93.9 million. Weak markets for pulp and lumber, a strong Canadian dollar and high wood costs all were negative factors which created this most unsatisfactory result. Our financial results would have been even worse had it not been for the efforts of the people throughout Canfor and our joint venture affiliates who worked diligently to hold costs down, develop new products, find new customers and continue to satisfy existing customers. We hope the information contained in this report will provide our shareholders and others with a meaningful discussion and analysis of the Company's performance and future prospects.

Roy A. Bickell retired as President and Chief Operating Officer in October 1991. Arild S. Nielssen, previously Vice-President, Interior Operations was appointed President and Chief Operating Officer upon Mr. Bickell's retirement. At the same time, the Company was organized into three major business groups — Coastal Operations, Northern Wood Products, and Pulp and Paper headed by the following respective Group Vice-Presidents — Sheldon T. Stoilen, Peter J. Ashby and Christer A. Arnesen. This structure brings together within each group the key functions of wood supply, operations and marketing, thus positioning the Company to compete more effectively in world-wide markets.

Subsequent to the year-end, J. Robert Bickell retired as Vice-President, Wood Products, Northern B.C. and Wayne B. Jacques left the Company as Vice-President, Alberta Operations. In January 1992, Brian F. King joined Canfor as Vice-President, Human Resources.

I am pleased to welcome Arild S. Nielssen as a director of the Company. Mr. Nielssen was elected by the Board following Roy A. Bickell's retirement. I am pleased as well that all the present directors of the Company will stand for re-election at the forthcoming 1992 annual general meeting.

On behalf of the directors,

Peter J. G. Bentley
Chairman and Chief Executive Officer
March 5, 1992
Vancouver, British Columbia

Canfor Corporation

Annual Information Form

Information in this Annual Information Form
is as of December 31, 1991
unless otherwise indicated

Financial Highlights

	1991	1990[1]
Sales and income *(in millions of dollars)*		
Net sales	**$ 822.5**	$ 884.4
Income (loss) before extraordinary items	**(99.1)**	3.8
Net income (loss)	**(93.9)**	3.8
Cash flow *(in millions of dollars)*		
Cash flow from operations before interest and income tax	**$ (16.3)**	$ 118.2
Interest	**(26.2)**	(20.7)
Income tax	**6.3**	(2.6)
Per common share *(in dollars)*		
Income (loss) before extraordinary items	**$ (4.18)**	$ 0.07
Net income (loss)	**(3.96)**	0.07
Cash flow from operations before interest and income tax	**(0.76)**	5.08
Common shareholders' equity	**21.70**	25.90
Financial position *(in millions of dollars)*		
Working capital	**$ 86.5**	$ 135.5
Total assets	**1,219.3**	1,208.4
Long-term liabilities	**292.8**	242.0
Shareholders' equity	**585.8**	616.6
Total capitalization	**1,020.9**	1,048.4
Additional information		
Return on capital employed	**(7.6)%**	1.5%
Return on common shareholders' equity	**(16.7)%**	0.3%
Ratio of current assets to current liabilities	**1.4:1**	1.8:1
Ratio of total debt to shareholders' equity	**36:64**	28:72
Capital expenditures *(in millions of dollars)*	**$ 46.1**	$ 105.3
Number of employees at year-end	**4,317**	4,530
Employment costs *(in millions of dollars)*	**$ 233.0**	$ 232.9

Quarterly Financial Information

	1991				1990			
	1st	**2nd**	**3rd**	**4th**	1st	2nd	3rd	4th
Sales and Income *(in millions of dollars)*								
Net sales	**$ 213.6**	**$ 214.0**	**$ 205.9**	**$ 189.0**	$ 239.7	$ 236.7	$ 196.6	$ 211.4
Income (loss) before extraordinary items	**(16.5)**	**(15.7)**	**(34.5)**	**(32.4)**	13.1	30.5	(13.7)	(26.1)
Net income (loss)	**(10.7)**	**(15.7)**	**(34.5)**	**(33.0)**	13.1	30.5	(13.7)	(26.1)
Per Common Share *(in dollars)*								
Income (loss) before extraordinary items	**(0.75)**	**(0.71)**	**(1.42)**	**(1.30)**	0.55	1.31	(0.62)	(1.17)
Net income (loss)	**(0.50)**	**(0.71)**	**(1.42)**	**(1.33)**	0.55	1.31	(0.62)	(1.17)
Dividends paid	**—**	**0.20**	**—**	**0.25**	—	0.35	—	0.20

[1] *Certain 1990 figures have been restated to conform with the 1991 presentation.*

See page 50 for the definition of selected financial terms.

Five Year Summary

	1991	1990	1989	1988	1987
	(in millions of dollars)				
Net sales	**$ 822.5**	$ 884.4	$ 921.2	$1,084.2	$1,244.9
Income (loss) before extraordinary items	**(99.1)**	3.8	96.4	101.6	106.0
Net income (loss)	**(93.9)**	3.8	96.4	180.0	102.7
Total assets	**1,219.3**	1,208.4	1,270.0	1,159.9	921.5
Net cash	—	—	32.8	68.7	43.5
Net short-term indebtedness	**55.6**	10.4	—	—	—
Long-term indebtedness[(1)]	**271.8**	230.4	245.6	123.8	167.3
Redeemable preferred shares	**24.5**	25.0	25.0	75.0	75.0
	(dollars per common share)				
Income (loss) before extraordinary items	**$ (4.18)**	$ 0.07	$ 3.98	$ 4.21	$ 4.41
Net income (loss)	**(3.96)**	0.07	3.98	7.67	4.26
Dividends paid	**0.45**	0.55	0.70	0.55	0.35

(1) *Includes current portion.*

The following factors affect the comparability of the data in the above five year summary of financial data.

1991

Costs of $5 million were accrued in 1991 in connection with the reduction of the hardboard panelling line and the restructuring of the operations of the Panel and Fibre Division in New Westminster, British Columbia to be effected in April 1992.

On August 1, 1991, Canfor completed a public distribution of 3 million common shares for net proceeds of $75.0 million.

1990

On April 30, 1990, Canfor sold its High Level Division, comprising a sawmill and related logging operations at High Level, Alberta. In February 1991, Canfor closed its plywood mill at Grande Prairie, Alberta. The estimated costs of $6.3 million relating to the closure were accrued in 1990.

1989

On February 1, 1989, Canfor sold its building materials distribution operations to Canfor-Weldwood Distribution Ltd., of which it owns 50 per cent. The results of that company are included in Canfor's results on an equity basis.

On May 19, 1989, Canfor acquired Balfour Forest Products Inc. as a wholly-owned subsidiary and since then its results have been included in Canfor's results on a consolidated basis.

1988

On March 31, 1988, Canfor sold its Howe Sound Pulp and Westcoast Cellufibre Divisions to Howe Sound Pulp and Paper Limited, of which it owns 50 per cent. The results of that company are included in Canfor's results on an equity basis.

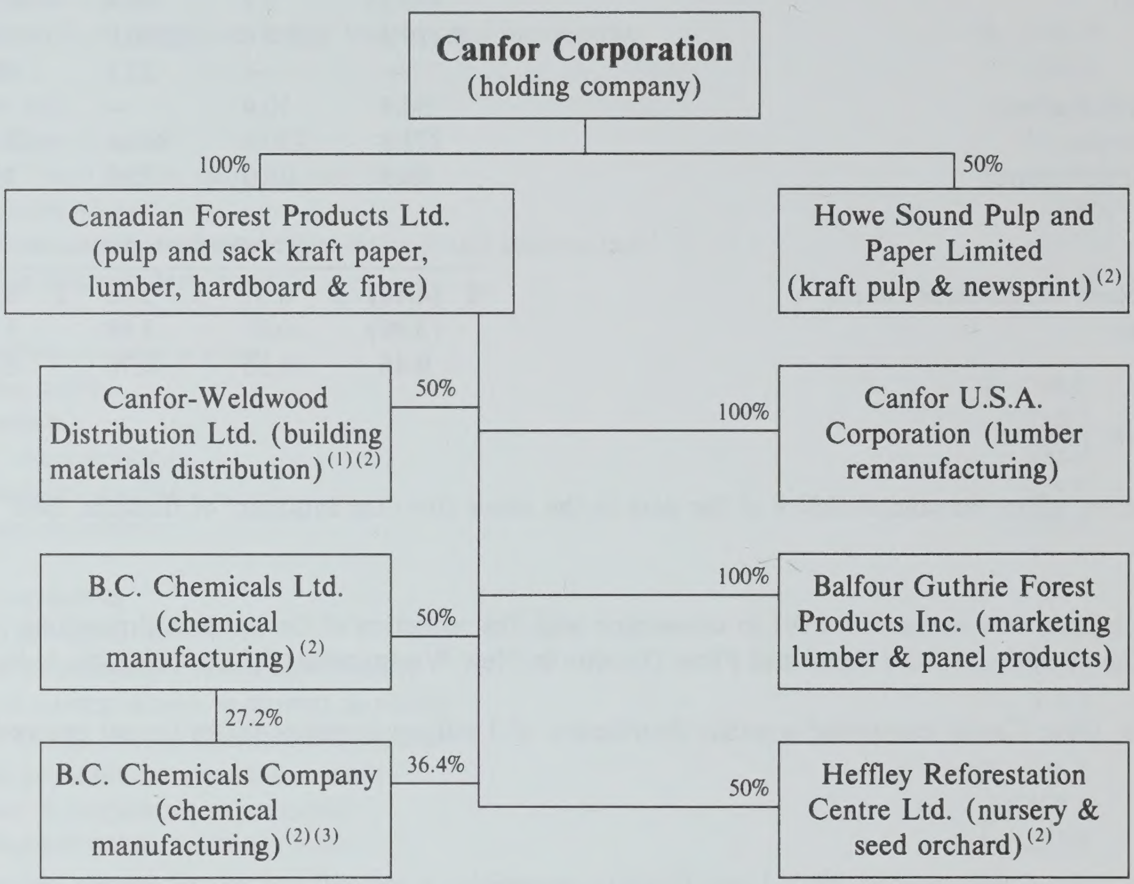
Incorporation

Canfor Corporation (the "Company") was incorporated on May 17, 1966, under the laws of the Province of British Columbia as part of a reorganization of predecessors of the Canfor group of companies, the first of which commenced operations in 1938. In July 1983, Canfor became a public company and the Common Shares of the Company are now listed on the Toronto and Vancouver stock exchanges.

The registered and principal office of the Company is located at 3000 – 1055 Dunsmuir Street, Vancouver, British Columbia. In this annual information form Canfor Corporation is referred to as the "Company" and, unless otherwise indicated by the context, "Canfor" refers to the Company and its subsidiaries.

Corporate Structure

The following chart shows the Company's principal operating subsidiaries and significant interests in other companies, their primary products or activities and the percentage of voting securities or ownership held by the Company. All of these companies are incorporated in British Columbia, except Heffley Reforestation Centre Ltd., which is incorporated under the Canada Business Corporations Act; Canfor U.S.A. Corporation, which is incorporated in Idaho, U.S.A; and B.C. Chemicals Company, which is an unincorporated joint venture enterprise.



(1) *Canfor-Weldwood Distribution Ltd. owns and operates on a combined basis the wholesale building materials distribution businesses formerly separately owned and operated by Canfor and Weldwood of Canada Limited.*

(2) *These companies, in all of which Canfor has a 50 per cent equity and voting interest, are referred to as "affiliates" or "affiliated companies".*

(3) *B.C. Chemicals Company is an unincorporated enterprise operated with B.C. Chemicals Ltd. and Northwood Pulp and Timber Ltd. Canfor's equity interest directly and through its interest in B.C. Chemicals Ltd. is 50 per cent.*

In addition, Canfor has a minority interest in Seaboard Shipping Company Ltd. ("Seaboard Shipping") which is owned by a group of British Columbia forest products companies including Canfor. Seaboard Shipping ships a portion of Canfor's lumber to overseas customers.

Up to December 1991, Canfor marketed a portion of its lumber to overseas customers through Seaboard Lumber Sales Ltd. ("Seaboard") in which it holds a minority interest. As discussed further under Business of Canfor — General Development, Canfor chose to withdraw from Seaboard Lumber and market all of its lumber for overseas customers through its subsidiary, Balfour Guthrie Forest Products Inc. As the result of this decision, Canfor is presently negotiating the disposal of its shares in Seaboard Lumber with the other shareholders.

Business of Canfor

General Development

Canfor is a Canadian integrated forest products organization employing approximately 4,300 persons in its wholly-owned forest products operations. In addition, Canfor's affiliates employ approximately 1,550 persons. Canfor holds extensive timber resources and carries on logging operations to provide raw material for processing at its manufacturing plants in British Columbia and northern Alberta. It also operates lumber remanufacturing plants in Idaho

and Washington State. The major products of Canfor and its affiliates are pulp, sack kraft paper, newsprint, lumber and hardboard. A significant portion of Canfor's products is exported to the United States, Europe and the Far East. Canfor maintains pulp and paper sales offices in Vancouver, Brussels, and Tokyo and a wood products sales office in London. Canfor-Weldwood Distribution Ltd. ("CanWel"), which Canfor owns jointly with Weldwood of Canada Limited, operates building materials distribution centres across Canada. The following briefly describes the significant developments which have taken place over the past five years.

1991

In January 1991, Canfor permanently reduced the operation of its sawmill at Taylor, British Columbia to a one shift per day basis, from two shifts, as the result of insufficient allowable annual cut on a long-term basis to meet the needs of both the Taylor and Fort St. John sawmills, which share the region's timber supply.

In February 1991, Canfor closed its plywood mill at Grande Prairie, Alberta as the result of increasing pressure from alternate products such as oriented strand board and a very poor future financial outlook for the plant.

In March 1991, Canfor completed construction of Canada's first plant for the production of wood fibre composite mat products. These products are a blend of refined wood fibre and various other fibres which can be pressed into three-dimensional products such as interior car panels and furniture components. After equipment fine-tuning and customer product development, commercial production of interior car panels commenced in November 1991.

In April 1991, Howe Sound Pulp and Paper Limited, which Canfor owns jointly with Oji Paper Co., Ltd. ("Oji") of Japan, commenced newsprint production at its new mill at Port Mellon, British Columbia. This portion of the expansion and modernization of the Howe Sound mill cost approximately $528 million. The newsprint is marketed by Oji primarily in Japan.

In July 1991, Canfor announced two major capital projects to upgrade the recovery boiler and install an oxygen delignification system at its Intercontinental pulp mill in Prince George, British Columbia. These projects, which are estimated to cost over $100 million and to be completed in mid-1994, represent significant steps forward in further improving the mill's environmental performance and in producing environmentally improved products being demanded by some market sectors.

In October 1991, Canfor announced it would be reducing its hardboard panelling product line and restructuring its operations at its Panel and Fibre Division in New Westminster, British Columbia, effective in April 1992.

As the result of its ownership of Balfour Guthrie Forest Products Inc., acquired in the purchase of Balfour Forest Products Inc. in 1989, Canfor chose, in December 1991, to withdraw from Seaboard Lumber Sales Ltd. Canfor had marketed the lumber from four mills in British Columbia and two mills in Alberta to overseas customers through Seaboard Lumber Sales Ltd. As the result of this change, all of Canfor's lumber for shipment offshore is now being marketed through its wholly-owned subsidiary Balfour Guthrie Forest Products Inc.

1990

On April 30, 1990, Canfor sold for $78.0 million its sawmill and related logging operations at High Level, Alberta to High Level Forest Products Ltd., a subsidiary of Daishowa Canada Co. Ltd. At the same time, Canfor entered into an agreement to market on an agency basis the lumber production of High Level Forest Products Ltd.

In June 1990, a modernization of Canfor's Eburne Sawmills Division at a cost of $25 million was essentially completed and the mill officially re-opened. As a result of the modernization, the mill has the capacity to produce higher value specialty products for offshore markets, including Japan.

1989

On February 1, 1989, Canfor and Weldwood of Canada Limited merged their respective building materials distribution divisions to form CanWel, a new, jointly-owned company.

In May 1989, Canfor acquired all of the shares of Balfour Forest Products Inc. for $93.75 million in cash. The acquisition added four sawmill operations with a total annual capacity of 600 million board feet, plus an overseas marketing operation for wood products, to Canfor's operations.

During 1989, Canfor formalized its long-standing commitment to being a leader in environment protection in Canada's forest industry. Canfor's environmental policy was officially announced in November and elaborates on Canfor's commitment to enhancement of the forest resource, responsible stewardship of the environment, and protection of human health and safety. Complying with or surpassing forestry, environmental health and safety regulations, and management of risks whether regulated or not are highlights of this comprehensive policy.

In April 1989, Canfor was granted Mill Licence No.5 by the Province of British Columbia, licensing Canfor to modernize and expand the capacity of its Prince George Pulp and Paper mills from approximately 1,600 air-dried tonnes of pulp per day to approximately 2,600 air-dried tonnes of pulp per day. This licensed expansion was intended to be

undertaken as an integral part of a project to make significant environmental improvements in the operations of the mills. As a result of the approximately 38 per cent drop in pulp prices in the 1990-1991 period and significant increases in productive capacity of market pulp throughout the world, the expansion has been deferred. Improvements to meet environmental standards and customer demand for chlorine-free pulp are presently being made at an estimated cost of approximately $110 million.

1988

On March 31, 1988, Canfor sold its Howe Sound Pulp and Westcoast Cellufibre Divisions to a new company, Howe Sound Pulp and Paper Limited ("Howe Sound"), which is jointly owned by Canfor and Oji for a total of $307.5 million paid in common and preferred shares. Howe Sound has subsequently, at a cost of approximately $1.1 billion, modernized and expanded the kraft pulp mill to produce approximately 954 tonnes of market pulp per day, has constructed, adjacent to the pulp mill, a newsprint mill with a capacity of approximately 585 tonnes per day together with a related thermo-mechanical pulp mill facility and is currently constructing a co-generation facility at an approximate cost of $142 million.

During the year, Canfor's Research and Development Centre was established to expand on the work successfully started by a small, highly qualified staff.

1987

The most significant external development in 1987 was the imposition by the Canadian Government of a 15 per cent export charge on softwood lumber exports to the United States. The export charge in British Columbia was replaced in November 1987 by increased stumpage fees and reforestation responsibilities established by the British Columbia Government. In 1991, charges for stumpage and reforestation costs in British Columbia totalled $54.7 million as compared to a total of $6.5 million in 1987. Of this $54.7 million, $21.8 million relates to the Balfour operations acquired subsequent to 1987.

During 1987, Canfor discontinued its building materials distribution activities in the United States and opened a lumber remanufacturing plant in Washington State.

Industry Segments

Canfor's operations can be divided into three basic segments: Pulp, Sack Kraft Paper and Newsprint; Wood and Wood Products, including lumber, hardboard, fibre and remanufactured lumber products; and Building Materials Distribution. Canfor operates in these segments directly through its wholly-owned operations and indirectly through its affiliated companies.

In addition, Canfor conducts woodlands operations to provide the wood fibre requirements of its manufacturing operations.

The following table sets forth, by industry segment, Canfor's consolidated sales revenues and its equity in the sales revenues of its affiliated companies for the last two years.

	Year Ended December 31 1991	1990
	(millions of dollars)	
Pulp, sack kraft paper and newsprint		
Canfor's consolidated sales	**$ 242.2**	$ 290.9
Equity in sales of affiliated companies	**95.9**	64.5
	338.1	355.4
Wood and wood products		
Canfor's consolidated sales		
— lumber	**491.1**	486.6[1]
— panel products	**57.4**	80.0
— chips and other	**31.8**	26.9[1]
	580.3	593.5
Equity in sales of affiliated companies	**0.6**	0.6
	580.9	594.1
Building materials distribution		
Equity in sales of affiliated companies	**208.0**	254.3
Canfor's consolidated sales	**822.5**	884.4
Equity in sales of affiliated companies	**304.5**	319.4
Canfor's consolidated sales and equity in sales of affiliated companies	**$1,127.0**	$1,203.8

[1] *These figures have been restated to conform with the 1991 presentation.*

The following table indicates the composition of Canfor's consolidated sales revenues by market for the last two years.

	Year Ended December 31 1991	1990
Canada	**17%**	16%
United States	**41**	44
Europe	**25**	28
Far East	**16**	11
Other	**1**	1
	100%	100%

Wood Supply

Timber Resources

Canfor harvests timber in British Columbia and northern Alberta to supply its manufacturing plants. Wood fibre requirements are also supplied by open market purchases and exchanges on either a spot or contract basis. Canfor owns timberlands and holds several types of forest tenures in the Provinces of British Columbia and Alberta which permit the harvesting of Crown timber. The following table sets forth Canfor's timber resources as at January 1, 1992.

	Productive Area (hectares)	Allowable Annual Cut (cubic metres)
British Columbia		
Tenures having regulated sustained yields		
Area-based		
Tree Farm Licences[1]	603,122	1,390,316
Volume-based		
Forest Licences	N/A	3,459,853
Tenures without regulated sustained yields		
Timber Licences	10,300	317,000[2]
Crown granted land (fee simple)	2,291	N/A[3]
Alberta		
Tenures having regulated sustained yields		
Forest Management Agreements	344,497	730,000[4]
Timber Quotas	N/A	202,498
Total	960,210	6,099,667

N/A denotes Not Applicable

(1) *Comprised of TFL 37 (Englewood) and TFL 48 (Chetwynd).*
(2) *Total inventory volume of 3,495,000 cubic metres to be depleted over the next 11 years.*
(3) *Total inventory volume of 372,000 cubic metres to be cut as needed.*
(4) *The allowable annual cut for the Alberta Forest Management Agreements has been recalculated and approved at 730,000 cubic metres.*

The Province of British Columbia owns approximately 95% of all timberlands in the province. Pursuant to the provisions of the Forest Act, the Minister of Forests is empowered to grant various forms of tenure and to regulate forestry operations. Tree Farm Licences may be granted to a licensee who undertakes to manage an area of Crown forest land, often in combination with other forest land held by the licensee, to yield an annual cut on a regulated sustained yield basis. A Tree Farm Licence is granted for a 25 year term and, subject to satisfactory levels of performance, may be replaced every ten years with a new Tree Farm Licence having a 25 year term.

The other major forms of tenure under which Canfor operates in British Columbia are Forest Licences and Timber Licences. Forest Licences are the standard volume-based tenure throughout the province and generally provide for 15 year terms. These licences may be replaced every five years for further 15 year terms, subject to satisfactory levels of performance. Timber Licences are a non-renewal form of tenure which the licensee surrenders to the Crown after the timber to which the licence applies has been harvested. In addition, under two Pulpwood Agreements with the Province of British Columbia, Canfor has the right to harvest pulpwood, if necessary, to supply the requirements of its two pulp mills at Prince George. The Pulpwood Agreements expire in 2008 and 2012 but are replaceable, prior to their expiry, under the Forest Act. Canfor has not needed to resort to its rights under these or their predecessor agreements since 1976.

Under Tree Farm Licences and Forest Licences an allowable annual cut is determined. The cut in any one year may be increased or decreased by Canfor by up to 50% of the annual volume specified, provided that the average cut over a five year period is within ten per cent of the specified volume for that period.

In northern Alberta, Canfor has a Forest Management Agreement under which it undertakes to manage an area of Crown forest land and which expires in 1998. This Forest Management Agreement provides for renewal every 20 years, on terms and conditions to be negotiated at that time. The Province of Alberta also grants Timber Quotas having terms of 20 years and containing provisions for renewal. These quotas are intended to provide a continuous supply of timber in perpetuity. Canfor has three such Timber Quotas which are scheduled for renewal in 2006.

Canfor's regulated sustained yield tenures in Alberta specify an allowable annual cut and an aggregate allowable cut over a five year period. The actual cut during each five year period must be at least 60% of the aggregate specified for that period for the tenure to remain in good standing. Canfor would be subject to significant levies if its production were to exceed 110% of the aggregate allowable cut for that period.

Canfor is in substantial compliance with the terms of its tenure agreements in British Columbia and Alberta.

Replacement of Canfor's Tree Farm Licence 37 was originally scheduled to occur on January 1, 1991, but has been delayed for up to three years as a result of amendments to the Forest Act. The Ministry of Forests has advised that it will not proceed with any Tree Farm Licence replacements until after completion of a review of certain recommendations contained in a report of the British Columbia Forest Resources Commission released in April 1991.

On January 21, 1992, the government of the Province of British Columbia announced that a Commission on Resources and the Environment would be formed by new legislation to develop and implement a process to create a land use plan for the province. The initial task of the Commission will be to resolve land use disputes in five specified forestry areas on Vancouver Island (none of which include tenures of Canfor). It is expected that the Commission will make recommendations for regional land use which will define both protected areas and working forest areas with the intent of doubling parks and wilderness areas. Further regional planning processes are expected to be initiated for other areas both on Vancouver Island and on the mainland. This Commission will also recommend provincial policies and legislation for land and water use.

The Government of British Columbia also announced that the Forest Resources Commission would propose a forest practices code. The announcement also indicated that the activities of the Commission on Resources and the Environment will support and not interfere with previously announced negotiations between the provincial government and representatives of the First Nations on aboriginal self-government treaties.

Forest Management

Canfor is responsible for all aspects of forest management on the lands it holds under Tree Farm Licences in British Columbia. In Alberta, Canfor is responsible for all aspects of forest management on the lands covered by its Forest Management Agreements, except forest fire protection, which is a responsibility of the Province of Alberta. The lands held under Tree Farm Licences, Forest Management Agreements, Forest Licences and Timber Quotas are managed on a sustained yield basis whereby the volume of timber harvested is regulated according to the productive capacity of the land and the inventory of mature timber available for harvest. In both British Columbia and Alberta, Canfor is responsible for reforestation of areas logged on all of its sustained yield tenures as well as on Timber Licences. The overall management of forest lands held under Forest Licences, Timber Quotas and Timber Licences is the responsibility of the respective Forest Services of British Columbia and Alberta.

Canfor carries out its forest management responsibilities through a staff of 48 registered professional foresters and forestry engineers. This forestry staff is engaged in supervising aspects of forest development including planning, road development, harvesting methods and forest protection, and in research and development programs to increase the yield of its forest lands and improve the quality of its timber resources. At Kamloops, British Columbia, Canfor and a joint venturer operate Heffley Reforestation Centre Ltd. as a source of planting stock. The Heffley facilities include a forestry seed orchard for genetic improvements and a forest seedling nursery. Canfor itself operates seed orchards at Sechelt, British Columbia and Grande Prairie, Alberta.

Canfor's forestry staff supervises the reforestation of all harvested areas which, in 1991, involved the planting of 21.4 million seedlings on 17,600 hectares, seeding of 1,200 hectares and natural regeneration of 2,400 hectares for a total of 21,200 hectares. This compares to 18,600 hectares harvested during 1991.

To protect the forest crop, Canfor maintains a fire prevention and suppression program in British Columbia. Surveillance to detect any forest infestation by insects and disease is carried out on a regular basis. Currently, Canfor is not experiencing any economically significant problems of this nature.

In response to growing public interest in environmental issues, Canfor sponsors public tours of its logging and forestry operations and seeks opportunities to ensure the public has full information at its disposal regarding Canfor's logging and forestry practices.

Wood Fibre Supply

The wood fibre supply for Canfor's and Howe Sound's wood products and pulp and paper operations is obtained by logging on Canfor's forest tenures and purchasing logs, chips and waste from the manufacture of wood products. Logs are purchased from other tenure holders and from farmers, native Indian bands and other private landholders. Chips and waste materials are purchased from sawmillers and other wood products producers. Often, Canfor sells logs that cannot be converted in its mills or Howe Sound's Westcoast Cellufibre operations to these sawmillers and other wood products producers, receiving chips and waste materials in exchange. The following table sets forth the volume of wood fibre produced and purchased, the volume of wood fibre consumed in Canfor's and Howe Sound's mills, and the volume of wood fibre sold to other wood fibre consumers for the last two years.

	Year Ended December 31	
	1991	1990
	(thousands of cubic metres)	
Production from timber tenures		
Coastal British Columbia	**1,623**	1,589
Northern Interior of British Columbia	**3,737**	3,940
Northern Alberta	**902**	730
Total production	**6,262**	6,259
Purchases		
Logs	**1,294**	1,022
Chips	**3,910**	1,880
Total purchases	**5,204**	2,902
Total production and purchases	**11,466**	9,161
Sales		
Logs(1)	**1,118**	992
Chips(2)	**1,324**	607
Total sales	**2,442**	1,599
Total available for conversion into finished goods	**9,024**	7,562
Total converted by Canfor operations into finished goods	**9,241**	7,462

(1) *Logs that cannot be converted in Canfor's mills or Howe Sound's Westcoast Cellufibre operations are sold to obtain chips and waste materials.*

(2) *Included in chip sales are 349,500 cubic metres (1990 — 386,700 cubic metres) of chips sold by the Alberta Operations where Canfor does not have a pulp mill and 106,260 cubic metres (1990 — 176,000 cubic metres) sold under a contract which pre-dates the Balfour acquisition.*

(3) *Waste materials used for fuel and hardboard furnish are excluded from this table because of the difficulty of determining a reasonable conversion factor to solid wood equivalent.*

Pulp, Sack Kraft Paper and Newsprint

Prince George Pulp and Paper Mills

Canfor is one of Canada's major producers of Northern Softwood Bleached Kraft ("NSBK") pulp for sale in the world market. Kraft pulp is raw material for paper manufacturing and is used in the production of printing and other fine paper, tissue, newsprint and paperboard. NSBK pulp imparts strength to the product in which it is used as the result of the length of its fibre. Canfor manufactures bleached, semi-bleached and unbleached kraft pulp at its Prince George Pulp and Paper and Intercontinental Pulp facilities located in Prince George, in the northern interior of British Columbia. In addition, Prince George Pulp and Paper produces sack kraft paper using pulp produced at its mill.

The operations of the Prince George Pulp and Paper and Intercontinental Pulp mills are located adjacent to each other, are jointly administered and have common pulp chip purchase arrangements. Sodium chlorate, which is used to make chlorine dioxide used in the pulp bleaching process, is supplied to these mills by B.C. Chemicals Ltd. in which Canfor owns a 50 per cent interest. Through B.C. Chemicals Company, an unincorporated venture enterprise among Canfor, Northwood Pulp and Timber Limited ("Northwood") and B.C. Chemicals Ltd., the sodium chlorate plant was

expanded and the crude tall oil plant was upgraded at an aggregate cost of approximately $60 million. This project has been financed without recourse to Canfor or Northwood.

The following table sets forth the daily and annual production capacities of Canfor's Prince George pulp and paper operations as at December 31, 1991.

	Daily capacity	Annual capacity[(1)]
	(tonnes)	
Kraft pulp		
Prince George Pulp and Paper	494	170,000
Intercontinental Pulp	688	235,000
Total capacity	1,182	405,000
Sack kraft paper		
Prince George Pulp and Paper	285	100,000

[(1)] *Assuming continuous operation for an average of 344 operating days per annum, rounded to the nearest 5,000 tonnes.*

Since 1989, the Prince George Pulp and Paper and Intercontinental Pulp mills have held quality assurance program registration under Canadian Standards Association (CAN3Z299.4 standard) and International Standards Organization (ISO9003 standard). These were the first pulp and paper mills in North America to achieve this registration. ISO 9000 is a series of international standards (with which CSA Z299 complies) which define those management elements that are essential to the establishment of an effective quality assurance system. Registration is only granted and maintained following successful completion of intensive, in-plant audits by certified independent quality auditors. Thus, registration under ISO 9000 confirms that those quality standards to which a company claims to adhere are, in fact, being maintained.

In response to the needs of some of their customers, the Prince George pulp operations introduced a grade of pulp in 1991 that has eliminated the use of elemental chlorine in the bleaching process.

As discussed more fully under Environment, Canfor's pulp operations have virtually eliminated dioxins and furans in their effluent and pulp and have reduced other chlorinated organic compounds well in advance of regulatory deadlines.

Howe Sound Pulp and Paper Limited

Howe Sound is owned as to 50 per cent by each of Canfor and Oji, a leading Japanese producer and marketer of paper, including newsprint. Howe Sound commenced operation in April 1988 when Canfor sold its Howe Sound Pulp division at Port Mellon, British Columbia and its Westcoast Cellufibre division at Vancouver, British Columbia to Howe Sound.

In late 1990, Howe Sound completed modernizing and expanding the kraft pulp mill to a capacity of approximately 954 tonnes of market kraft pulp per day and in April 1991 completed construction of a newsprint mill, adjacent to the pulp mill, with a capacity of approximately 585 tonnes per day together with a related thermo-mechanical pulp mill facility. A co-generation facility is presently being constructed to generate electrical power for the pulp and newsprint operations. The first turbine generator started operation in February 1991, the second turbine generator in January 1992 and supporting wood waste boiler and ancillary equipment will be in full operation in the latter half of 1992. The estimated cost of all of these improvements is $1.25 billion.

Under agreements which Howe Sound has with Canfor and Oji, Canfor supplies and obtains fibre for the mills at market prices, markets the pulp on a commission basis and provides certain management services for a fee related to cost. Oji provides Howe Sound with technical services, particularly in relation to the newsprint mill; Howe Sound reimburses Oji for the costs and expenses incurred in providing the services. Oji is responsible for marketing on an agency basis the newsprint production from Howe Sound, which will be sold primarily in Japan.

For the twelve months ended December 31, 1991, Howe Sound produced 226,918 tonnes of kraft pulp, significantly less than present capacity of 330,000 tonnes, because of start-up problems following the modernization and curtailments resulting from adverse pulp market conditions.

In the period from completion of construction of the newsprint mill in April 1991 to December 31, 1991, Howe Sound produced 86,099 tonnes of newsprint.

Howe Sound operates as a separate corporation. All of the financing which has been arranged by Howe Sound for the modernization and expansion is without recourse to Canfor or Oji. Canfor and Oji subscribed for $60 million each of preferred share capital of Howe Sound during 1991 and plans to subscribe for an additional $15 million in

February 1992. These funds were required to meet costs not originally planned which arose from the modernization and expansion project and to offset the financial effects of weakening of pulp markets and starting up the new and expanded facilities.

Production and Sales Summary

The following table sets forth pulp, sack kraft paper and newsprint production and sales statistics for Canfor's consolidated operations and its equity in Howe Sound for the last two years.

	Year Ended December 31	
	1991	1990
	(tonnes)	
Pulp Production		
Prince George Pulp and Paper	**154,108**	129,161
Intercontinental Pulp	**208,576**	197,037
Total consolidated production	**362,684**	326,198
Equity in the production of Howe Sound Pulp and Paper Limited	**113,459**	70,850
	476,143	397,048
Pulp Sales		
Consolidated sales	**372,271**	305,092
Equity in the sales of Howe Sound Pulp and Paper Limited	**114,744**	63,435
	487,015	368,527
Sack Kraft Paper Production	**90,788**	90,706
Sack Kraft Paper Sales	**89,462**	93,136
Newsprint Production		
Equity in the production of Howe Sound Pulp and Paper Limited	**43,050**[(1)]	—
Newsprint Sales		
Equity in the sales of Howe Sound Pulp and Paper Limited	**34,365**	—

(1) *Start-up of the newsprint machine commenced in April 1991*

During 1991 and 1990 the Prince George Pulp and Intercontinental Pulp mills were curtailed in total for 53 and 120 days respectively because of the decline in pulp prices and demand resulting from depressed economic conditions. Similarly, Howe Sound took 21 days of market curtailment in 1991 and 48 days in 1990. In addition, Howe Sound's 1990 production was reduced by construction work on the mill modernization and expansion project.

Pulp and Sack Kraft Paper Marketing and Distribution

Canfor, through its Canfor Pulp and Paper Marketing Division sells the pulp and sack kraft paper production of its Prince George Pulp and Paper mills and Howe Sound under an agency agreement in international markets. Pulp and paper sales offices are presently maintained in Vancouver, Canada; Brussels, Belgium; and Tokyo, Japan. In addition, Canfor is represented by pulp and paper sales agents serving various other markets around the world.

In 1991, the approximate geographic distribution of pulp sales was 57 per cent to the European market, 26 per cent to the Far East, 13 per cent to North America and four per cent to various other markets. The distribution of sack kraft paper sales in 1991 was 26 per cent to Europe, 57 per cent to North America, 12 per cent to the Far East and five per cent to other markets.

Canfor uses various modes of surface transportation to distribute the pulp and paper products it sells. From the Prince George mills, North American markets are served by both rail and truck carriers. Export markets are served by rail or truck to Vancouver or Squamish, British Columbia and then via dedicated vessels to major markets in Europe, Japan and Korea. Other markets such as Mexico and China and other countries in Southeast Asia are served by modern, small multi-cargo vessels or container carriers.

Canfor is able to load containers at its mills for delivery directly to its customers' mills in many of the markets it serves. Modern forest product terminals at Vancouver and Squamish are used for transferring pulp and paper products from rail cars and trucks to vessels. At Port Mellon, Howe Sound has rail facilities, container facilities and has its own deep-sea dock, where vessels load directly.

Newsprint Marketing and Distribution

Oji, a leading Japanese producer and marketer of paper, including newsprint, is responsible for the marketing and distribution of the newsprint production of Howe Sound. The deep-sea dock and container facilities at Port Mellon are utilized in shipping the newsprint by vessel to Japan and other overseas markets. Howe Sound's rail facilities are utilized for those shipments to the North American market.

The geographic distribution of newsprint sales in 1991 was 35 per cent to Japan and the balance, which was primarily produced during the period of mill start-up and fine-tuning to meet Japanese market specifications, was sold in the North American and Asian markets.

Pulp and Sack Kraft Paper Markets and Competitive Position

Over the long term, global consumption of paper and board is anticipated to continue to expand at a rate in excess of the general expansion of the economy. It is expected that substantial additional quantities of paper-making fibres will be required, and Canfor is well placed to participate in this growth.

As the result of increased pulp capacities and use of recycled fibres and fillers, market pulp capacity utilization ratios in the early 1990's are expected to be lower than in the second half of the 1980's. The extent to which recycled fibres and fillers will displace virgin fibre is presently a matter of uncertainty in the industry. However, Canfor's management believes that it will be the weaker and shorter fibre from mechanical and hardwood pulps which will be most affected by this displacement. Since the long fibres from chemically produced NSBK pulp, Canfor's grade of pulp, impart strength to paper, Canfor's management believes that NSBK pulp will suffer less displacement than will other grades.

Pulp prices through most of 1991 continued the decline which commenced in 1990 as the result of the addition of new pulp capacity, lower demand arising from the current slow-down in the world economy and papermakers keeping their pulp inventories at minimum levels in anticipation of greater supply and lower prices. Whereas in 1990 the prices for pulp grades other than NSBK pulp fell faster than prices for NSBK pulp, during 1991 the price for NSBK pulp fell more rapidly than for other grades. The result was the re-establishment of the historical price differentials to other pulp grades in the second half of 1991. This induced greater demand for NSBK pulp which, coupled with some improvement in economic conditions, resulted in increased shipments of all pulp grades and some price recovery late in the year. Canfor's management believes the price recovery will continue in 1992 and thereafter as markets throughout the world adjust to absorb the recent increases in pulp productive capacity.

The pulp mills of Canfor and Howe Sound are well positioned within Canada with regard to fibre supply, environmental performance, energy supply and a skilled work force. Their competitive position will be further enhanced by the major investments currently being undertaken and recently completed. With these new investments Canfor is very well positioned to meet the rapidly expanding demand in Europe for pulps bleached without the use of elemental chlorine or any chlorine compounds at all. Howe Sound was the first kraft mill in North America to complete successfully a full scale mill trial of completely chlorine-free, market pulp in commercial quantity late in the year. At Canfor's mills in Prince George, similar trials are scheduled for the first quarter of 1992. Canfor's management believes that markets in Europe will demand these new grades and the company is in the forefront of North American suppliers in meeting this demand.

The competitive position of Canadian producers, relative to European producers, is dependent to a significant extent on the relationship between the various currencies in which pulp is sold. In 1990 and 1991, the relatively high value of the Canadian dollar vis-a-vis the United States dollar significantly reduced net prices to the mills.

Over the last few years, markets for sack kraft paper have continued to decline, but at a slower pace than in the past. The industry has enjoyed generally good operating rates, allowing prices to remain stable as many machines have ceased to make brown grades. A further reduction in demand is anticipated, and ongoing elimination of capacities will be required to allow good operating rates and stable pricing. Some existing capacity will be converted to make recycled packaging grades, which is in increasing demand in the grocery bag segment. A limited usage of recycled fibres in multi-wall grades can also be expected, but to a much lesser extent than in the grocery bag application.

In contrast to the general decline, Canfor's kraft paper sales increased in 1991 as a reflection of the high level of quality and service offered to customers. Canfor has established itself as a premium sack kraft paper producer in the United States market, and is well considered in other parts of the world. This niche marketing adds to Canfor's competitiveness.

Newsprint Markets and Competitive Position

The newsprint market in Japan has for several years been growing at a more rapid rate than that of other industrialized countries. It is also the most quality conscious newsprint market in the world. As the result of this high quality standard, very few foreign newsprint manufacturers have succeeded in gaining the confidence of the Japanese publishers to achieve access to this very attractive and promising market. Howe Sound's newsprint mill was designed, constructed and is being operated specifically to meet this Japanese quality standard. With extensive technical, operational and sales assistance from Oji, Howe Sound newsprint has already been accepted by many Japanese publishers even though the mill is still in its start-up phase and still undergoing fine-tuning. As the result of the achievement of Japanese standard early in the start-up phase of the mill, more than one-third of 1991 newsprint shipments were to Japan, with the balance sold mainly in North America and Asia. Because of its exceptionally high quality, Howe Sound's newsprint has been well accepted and appreciated by quality conscious customers in those markets. This acceptance has resulted in Howe Sound being able to sell its production in spite of the current oversupply situation which is depressing newsprint markets throughout the world.

Human Resources

Canfor employs approximately 990 persons in its Prince George Pulp and Paper mills and Canfor Pulp and Paper Marketing Division, of whom 70 per cent are covered by collective agreements with the Pulp, Paper and Woodworkers of Canada and the Canadian Paperworkers unions. Howe Sound employs approximately 890 persons, of whom 75 per cent are covered by a collective agreement with the Canadian Paperworkers Union. The collective agreements which expired on June 30, 1991 were extended for ten months to expire in April 1992. Negotiations for the renewal of these contracts are expected to commence in March 1992.

The safety of its employees has always been a primary concern at Canfor. For 1991, according to statistics compiled by the Pulp and Paper Industrial Relations Bureau, the Intercontinental Pulp mill was the safest pulp mill in British Columbia, closely followed by the Prince George Pulp and Paper mill which ranked third and Howe Sound which ranked sixth out of 20 mills.

Wood and Wood Products

Lumber

Canfor's 1991 lumber production totalled 1.35 billion board feet, ranking it as one of the largest lumber producers in the world. Currently, Canfor operates eight sawmills in the interior of British Columbia and two sawmills in Alberta. Dimension lumber is produced at five sawmill operations in the interior of British Columbia and one sawmill in Alberta, while studs (generally eight foot length two by fours) are produced at one mill in Alberta and three mills in the interior of British Columbia. Canfor has one coastal sawmill (Eburne) which produces a variety of hemlock products. The sawmills produce wood chips from the portion of each log not converted into lumber. These chips are sold to pulp mills as their raw material.

Canfor operates lumber remanufacturing, finger-joint, joinery, edge-gluing and laminating facilities to improve profit margins on lumber that would otherwise yield lower returns. Lumber remanufacturing facilities having a combined capacity of 135 million board feet are operated by Canfor's United States subsidiary, Canfor U.S.A. Corporation, at Meridian, Idaho, and Bellingham, Washington. Canfor operates a joinery plant and a finger-joint plant in conjunction with two of its sawmills in the interior of British Columbia.

Edge-glued boards are produced at Canfor's Meridian, Idaho, plant and laminated lumber is produced at the Specialty Products Division (formerly Canfor Research and Development Centre's pilot plant) in Vancouver, British Columbia.

Canfor's mills have an aggregate annual productive capacity of approximately 1.5 billion board feet, on a basis of two shifts per day and 240 operating days per year. The following table sets forth Canfor's lumber production and sales for the last two years.

	Year Ended December 31	
	1991	1990
	(MFBM)*	
Coastal British Columbia	**51,515[(1)]**	40,649[(1)]
Northern Interior of British Columbia	**1,101,677[(4)]**	1,118,497[(2)]
Northern Alberta	**200,687**	271,895[(3)]
Total production	**1,353,879**	1,431,041
Sales	**1,336,430**	1,388,311

**Mfbm denotes thousand foot board measure*

(1) *Production was curtailed at the Eburne mill in early 1990 because of a mill modernization project in progress and during 1990 as the result of start-up problems in the mill. Production was curtailed for 185 shifts (out of 480 normal shifts) during 1991 primarily as the result of market conditions and some operating problems in the mill.*

(2) *The Northern Interior mills curtailed operations for two weeks during 1990 to avoid building excessive chip inventories during curtailments at Canfor's pulp mills.*

(3) *The High Level mill was sold on April 30, 1990.*

(4) *In January 1991, the operation of the Taylor mill was reduced to a one shift per day basis.*

Lumber Distribution

Canfor markets its lumber throughout North America and overseas. Canfor's Wood Products Marketing Division in Vancouver, British Columbia markets Canfor's lumber production throughout North America. In addition, Canfor markets lumber on an agency basis for two other producers. In 1991, approximately 68 per cent of Canfor's sales of lumber was made directly into the United States market, of which virtually all was shipped by rail and truck. To assist in transporting its products to the United States, Canfor has available a fleet of approximately 1,140 leased railway cars. Sales to Canadian customers accounted for approximately 20 per cent of total sales and an additional 12 per cent of sales was made to overseas customers, principally in Europe and the Pacific Rim.

Following the acquisition of Balfour Forest Products Inc. in 1989, Canfor terminated its offshore lumber marketing through Seaboard Lumber Sales Ltd. in December 1991 and now all sales to overseas customers are made through Balfour Guthrie Forest Products Inc., a wholly-owned subsidiary. Balfour also markets to overseas customers lumber and panel products from a number of independent mills in Canada and the United States. Balfour maintains sales offices in Vancouver, British Columbia and the United Kingdom. Arrangements for shipments to overseas customers are made either through Seaboard Shipping or various other shipping lines.

Lumber Markets and Competitive Position

The North American marketplace continued to be very difficult in 1991 as the result of a continuation of lumber supply exceeding demand. New housing starts declined in the United States by 15 per cent and in Canada by 14 per cent. These declines followed the declines in 1990 of 17 per cent and 16 per cent respectively. A slowing of demand in offshore markets further exacerbated this situation.

The 1992 outlook for lumber sales, both in North America and offshore, is significantly more positive than for the previous two years. Lumber prices in North America are expected to firm at higher levels as the result of a combination of factors; increase in demand; reduced supply arising from withdrawals of timber for environmental reasons; and closure of mills arising from the economic conditions experienced in the last two years. Offshore demand for lumber is expected to be generally favourable in 1992, with improvement expected in the key United Kingdom market and much slower, but still positive, demand growth forecast for Japan and Germany.

Although uncertainty and less than desirable economic growth are expected to continue in all markets in 1992, the spruce/pine/fir (SPF) segment of the market, which accounts for 90% of Canfor's production, is expected to gain in market share as the result of several factors. SPF has recently gained greater acceptance in industrial markets as the result of recognition of higher strength values. In Japan, buyers are turning increasingly to SPF as log imports decline from Southeast Asia, the Pacific Northwest of the United States and the Commonwealth of Independent States (formerly the Soviet Union). European customers are spurning tropical hardwoods for environmental reasons. They are

also demanding that softwood lumber be kiln-dried. Canfor kiln dries all of its SPF production and has drying capacity for coastal fir and hemlock greater than its present level of sales to the European market.

Canfor's approach to the changes it perceives in the global marketplace is to strive for the most profitable balance between commodity products and specialty products that meet the needs of specific end-users. This involves improving the quality of commodity lumber and increasing the proportion of specialty products through such programs as the addition of new grades and dimensions, species sorting, greater attention to moisture content and further processing to meet the needs of specific customers. Canfor's management believes this matching of the commodity/specialty product mix to the quality potential of Canfor's timber base and its commitment to satisfying specific customer needs is the key to its future profitability in lumber.

Canfor supports this commitment through placing a strong emphasis on forming a long-term relationship with its customers, offering continuity of supply and customer service programs to compete in key markets. In the North American market, this emphasis has enabled Canfor to become a preferred supplier to a number of major retail lumber chains. Direct sales to industrial customers in both North America and overseas have also benefited from this emphasis on customer relations. In overseas markets, the emphasis on customer service combined with improvements in grading and manufacturing practices and Canfor's ability to satisfy specific customer needs has resulted in increased Japanese, European and specialty products orders.

For the next several years, tight timber supplies will be a dominating concern within the wood products industry. However, Canfor has access to one of the largest SPF supply bases and milling capacities in Canada. This places Canfor in a good position to continue its thrust and maximize return on its timber base. With intensive marketing of its products to key North American retail customers, a growing emphasis on Japanese and European markets and an increased focus on industrial customers, Canfor expects to continue to expand its role in the production and marketing of lumber.

Hardboard

Canfor operates a hardboard plant at its Panel and Fibre Division in New Westminster, British Columbia which principally utilizes purchased waste fibre as raw material. Most of Canfor's hardboard is finished to produce simulated woodgrain panels, embossed panelling and industrial products. This facility has a productive capacity of 40 million square feet (⅜ inch equivalent) per annum and is the only hardboard plant in western Canada.

The following table sets forth Canfor's production and sales of hardboard for the last two years.

	Year Ended December 31	
	1991	1990
	(millions of sq.ft. ⅜" equivalent)	
Hardboard		
Production	**33.9**	35.8
Sales	**35.6**	36.9

In October 1991, Canfor announced plans to reduce its panelling product line and restructure its hardboard operation. The changes, which will be effective in April 1992, will include the installation of a new natural gas-fired energy system and the elimination of those product lines which generate unsatisfactory profit contributions. Upon completion of this restructuring, productive capacity of the hardboard facility will be 25 million square feet (⅜ inch equivalent) per annum.

Hardboard Markets

In 1991, 63 per cent of hardboard sales were made in Canada, primarily to CanWel and 31 per cent was sold directly to the United States market. The balance was sold offshore in European and Pacific Rim markets. North American demand for hardboard was weak during 1991, as the result of the economic recession in North America, and improvement in demand will depend upon the extent of economic recovery in 1992.

Refined Fibre

In order to expand and diversify the range of products manufactured from its raw material base, Canfor has introduced two specially refined wood fibre products, baled fibre and Ecofibre, which are produced by the Panel and Fibre Division in New Westminster, British Columbia.

Baled, refined dry fibre is produced from wood residues and chips which are refined utilizing the hardboard mill's refining capacity, dried and compressed into highly compacted bales for easy handling and shipping. The fibre is used as raw material for hardboard production and in the manufacture of moulded products for the automotive industry. Most of Canfor's production in 1991 was sold in Japan and other Pacific Rim markets.

Ecofibre is refined dry fibre to which a non-toxic, environmentally safe green dye is added to yield a product which, when mixed with grass seed, fertilizer and water, can be sprayed on ground, in a process called hydro-seeding, as a fast and economical way of returning a disturbed surface area to a natural state.

Wood Fibre Composite Mat Products

In 1991, Canfor completed construction of Canada's first plant to manufacture wood fibre composite mat products. Wood fibre composite mats, which look like thick, flexible carpet, are a blend of refined wood fibre and various other fibres. They can be pressed into three-dimensional shapes to make a range of products including interior car panels and furniture components. Pressed wood fibre mats have a hard, smooth finish which can be covered with cloth, paint, veneer or other materials. The mats can also be engineered to meet the special performance requirements of different products, such as high strength-to-weight ratio and fire, water, or corrosion resistance. Fibre mats compete with plastics, metals and other industrial raw materials.

Equipment fine-tuning and trial runs commenced in March 1991. The plant is situated at the Panel and Fibre Division's New Westminster site and utilizes the existing infrastructure there. Canfor's investment in this composite mat facility and the related new product development is expected to be approximately $13 million upon completion of the product development phase. A non-interest bearing loan of $4.3 million from the Canadian and British Columbia governments was obtained to support the project through the start-up and product development phase.

Following customer testing and acceptance, commercial production of interior door panels for a major automobile manufacturer commenced in November 1991 and Canfor anticipates that further orders will stem from the success of this product.

Human Resources

Canfor employs approximately 2,660 persons in its Wood and Wood Products operations in British Columbia, 330 persons in its operations in Alberta and 136 persons in its operations in the United States. Of these, 71 per cent are covered by collective agreements with the International Woodworkers of America and the Canadian Paperworkers unions which, in the case of the British Columbia operations, expired in June 1991 and in the case of the Alberta operations, expire in February 1992. Negotiations for the renewal of the contracts which expired in June 1991 are currently in process and a satisfactory settlement is anticipated.

Building Materials Distribution

On February 1, 1989, Canfor and Weldwood of Canada Limited ("Weldwood") merged their respective Canadian building materials distribution divisions to form Canfor-Weldwood Distribution Ltd. ("CanWel"), a new, independent company owned equally by Canfor and Weldwood. All the equipment, inventory, working capital and goodwill related to Canfor and Weldwood's building materials distribution businesses were transferred to CanWel for common shares and debt. While some rationalization has taken place subsequent to the merger, CanWel continues to serve all the major market areas across Canada.

CanWel continues to sell lumber and hardboard produced by Canfor, as well as lumber and panel products produced by Weldwood and a wide range of building materials of other manufacturers. The majority of sales are to building supply outlets and industrial users. CanWel is the largest national distributor of building materials in Canada, enjoying greater efficiency and more secure sources of supply than either of the original organizations.

Canfor accounts for its interest in CanWel using the equity method. As a result, Canfor's income statement excludes revenues and expenses related to building materials distribution subsequent to January 31, 1989, but includes 50 per cent of CanWel's financial results.

It is intended by Canfor and Weldwood that CanWel operate as a separate corporation, that capital be generated from operations and that any additional capital required be obtained by borrowing without recourse to Canfor or Weldwood. However, during 1990, in order to strengthen CanWel's financial position against the developing recession in Canada, Canfor and Weldwood each converted $5.0 million of long-term advances to CanWel to share capital and converted $10.0 million of advances previously made on a short-term, interest bearing basis to a long-term, interest bearing basis on which interest is currently being waived.

The following table sets forth the building materials distribution sales for the last two years.

	Year Ended December 31	
	1991	1990
	(millions of dollars)	
Equity in sales of CanWel[1]	**$208.0**	$254.5

[1] *The equity in sales of CanWel is not included in Canfor's consolidated net sales.*

Markets and Competitive Position

CanWel markets a broad range of commodity and specialty products to retail building supply dealers and industrial fabricators throughout Canada. CanWel is the largest distributor of building materials in Canada, with over 100 major product lines, 22 combined distribution centres and sales offices in strategic locations and over 5,000 active customers. The product lines are balanced relatively equally between commodity wood products and specialty building materials in order to benefit from both new construction and repair and remodelling markets.

The market for building materials in Canada is cyclical and subject to the level of new housing starts, which are, in turn, strongly influenced by the level of interest rates and general economic activity. The repair and remodelling segment of the market is less cyclical than new construction but is also strongly influenced by the level of interest rates and general economic activity. During 1991, new housing starts in Canada declined 14 per cent, from 181,000 units in 1990 to 156,000 units in 1991. However, the housing start rate increased in each quarter of 1991 as interest rates declined.

Management of Canfor expects market conditions for building materials to continue to improve gradually in 1992, as the economy slowly recovers and rebuilds.

Environment

Canfor's environmental policy expresses its commitment to the enhancement of the forest resource on which it depends, to responsible stewardship of the environment in which it operates and to protection of the health and safety of its employees and the public.

Canfor meets this commitment by renewing, managing and protecting the forest resources for multiple use and sustained yield; by designing and operating its facilities to comply with or surpass environmental health and safety regulations; and by promoting environmental, health and safety awareness among its employees.

As described previously under Wood Supply — Forest Management, Canfor carries out its commitment to the renewal and enhancement of the forest resource through the leadership of its staff of registered professional foresters and forestry engineers. Canfor carries out its commitment to responsible stewardship of the environment through the leadership of its corporate and divisional environmental staff, and the diligence of its operating personnel. Environmental, health and safety awareness are promoted among Canfor's employees by various management supported initiatives.

The forest industry in Canada, and particularly in British Columbia, is facing tremendous public and regulatory pressure with respect to the environment. There are continuing concerns about dioxins and furans and other chlorinated organic compounds (measured as AOX) in the effluent from pulp mills using chlorine or chlorine-containing compounds for bleaching. In proposed federal regulations under the Canadian Environmental Protection Act, dioxins and furans in pulp mill effluent must be virtually eliminated by January 1, 1994. New federal pulp and paper mill effluent regulations have also been proposed under the Fisheries Act. The British Columbia Ministry of Environment, Lands and Parks has recently amended their pulp and paper mill effluent regulations, requiring mills in the province to meet a discharge limit of 1.5 kilograms AOX per tonne of bleached pulp production by December 31, 1995, and to eliminate AOX produced in the bleaching process by December 31, 2002.

Canfor's Prince George Pulp and Paper mills and Howe Sound have virtually eliminated dioxins and furans in their effluent and pulp, and are discharging less than 1.5 kilograms of AOX in their effluent per tonne of bleached kraft pulp produced. These mills also meet the proposed federal pulp and paper mill effluent regulations. This is significantly in advance of the regulatory deadlines.

There is growing demand, in certain markets where Canfor is active, for pulp with extremely low levels of chlorinated organic compounds, and for totally chlorine-free pulp. Customers that purchase forest products from Canfor are increasingly interested in our overall environmental performance.

In late 1991, Howe Sound became the first mill in North America and one of very few mills in the world to successfully produce medium brightness market kraft pulp in commercial quantity without the use of chlorine or compounds containing chlorine for bleaching.

In addition to addressing concerns about dioxins and furans and chlorinated organic compounds, Canfor is improving emissions at several of its facilities. Current projects include replacement of two old combination oil-wood fired boilers at Howe Sound in 1992 with a new co-generation woodwaste boiler, the replacement of two aging woodwaste boilers at its Panel and Fibre Division with natural gas fired boilers, and converting the recovery boiler at the Intercontinental Pulp mill in Prince George to a low odour recovery boiler.

On January 30, 1992, British Columbia's Minister of Environment, Lands and Parks announced the intention of the provincial government to substantially revise its existing environmental legislation over the next few years. Areas specified for new legislation were environmental impact assessments, fish and wildlife habitats, a comprehensive Environmental Protection Act to replace the existing Waste Management and Environment Management acts and revision of the Water Act.

The aggregate capital expenditures for environmental projects in 1991 was approximately $16.9 million.

Research and Development

Until 1980, Canfor's involvement in research and development was limited to its support of industry sponsored research organizations such as Forintek Canada Corporation and the Pulp and Paper Research Institute of Canada. Since that time Canfor has, in addition to its continuing support of these organizations, gradually increased its direct involvement in its own research and development programs. The objectives of Canfor's research and development efforts are:

(a) to work in conjunction with manufacturing and marketing in the development of new products, processes and services which, through greater or higher-valued utilization of available fibre, are aimed at enhancing Canfor's profitability and competitive position in the global market place, and

(b) to reduce the impact of Canfor's operations on the environment.

Pulp and paper research and development during 1991 focused on the elimination of chlorine-based bleaching agents in Canfor's pulp mills. This was successfully applied in a large scale trial at Howe Sound which resulted in the production of North America's first completely chlorine-free bleached softwood kraft pulp in commercial quantities for the market.

A laminated-wood pilot plant established in 1990 by Canfor's Research and Development staff to facilitate research in large-scale uses of low-quality and low-value wood materials for production of margin-added products was transferred to commercial operation in June 1991 and renamed the "Specialty Products Division".

Canfor's direct research and development expenditures, including capital expenditures, amounted to $3.6 million in 1991 and $4.5 million in 1990. While research efforts were expanded in 1991, overall expenditures declined from 1990 as the result of less spending on capital items.

Directors and Officers

Directors

The names and municipalities of residence of the directors of the Company, their principal occupations and the periods during which they have been directors of the Company are as follows:

Name and Municipality of Residence	Principal Occupation	Director Since
A.G. Armstrong, Q.C.(1) Vancouver, British Columbia	Senior Vice-President, Finance Canfor	1983
P.J.G. Bentley, O.C.(1)(3) Vancouver, British Columbia	Chairman and Chief Executive Officer, Canfor	1966
R.L. Cliff, C.M.(1)(2)(3) Vancouver, British Columbia	Chairman of the Board, BC Gas Inc	1983
C.W. Daniel, O.C. Toronto, Ontario	Corporate Director/Consultant	1985
M.H. Gunther(1) Vancouver, British Columbia	Vice-Chairman, Canfor	1983
B.R. Hislop Vancouver, British Columbia	Vice-President, Corporate Services, Canadian Forest Products Ltd.	1987
M.E. Hurst Vancouver, British Columbia	Educational Author	1987
J.B. Jarvis(1)(2) Vancouver, British Columbia	Corporate Director	1966
P.A. Lusztig(2) Vancouver, British Columbia	Former Dean, now Professor, Faculty of Commerce and Business Administration, University of British Columbia	1983
A.S. Nielssen(1) West Vancouver, British Columbia	President and Chief Operating Officer, Canfor	1991
M.E.J. Phelps(3) West Vancouver, British Columbia	President and Chief Executive Officer, Westcoast Energy Inc.	1990
R.T. Riley(3) Montreal, Quebec	Chairman of the Board, Chateau Insurance Management Inc.	1987

(1) *Member of the Executive Committee, which acts generally on behalf of the Board of Directors between meetings.*
(2) *Member of the Audit Committee, which reviews the Company's financial statements, the scope and results of the external auditors' work, the adequacy of internal accounting and audit programs and compliance with accounting and reporting standards.*
(3) *Member of the Management Resources and Compensation Committee, which makes recommendations to the board regarding the Company's pension plans and the remuneration of its directors and senior officers and ensures management development and succession programs are in place.*

The term of office of each director expires on the date of the next annual general meeting of the Company.

Officers

The names and municipalities of residence of the officers of the Company and the offices held by them are as follows:

Name and Municipality of Residence	Office and Principal Occupation
P.J.G. Bentley, O.C. Vancouver, British Columbia	Chairman and Chief Executive Officer
M.H. Gunther Vancouver, British Columbia	Vice-Chairman
A.S. Nielssen West Vancouver, British Columbia	President and Chief Operating Officer
A.G. Armstrong, Q.C. Vancouver, British Columbia	Senior Vice-President, Finance
C.A. Arnesen Lions Bay, British Columbia	Group Vice-President, Pulp and Paper
P.J. Ashby West Vancouver, British Columbia	Group Vice-President, Northern Wood Products
S.T. Stoilen Vancouver, British Columbia	Group Vice-President, Coastal Operations
J.R. Bickell(1) Prince George, British Columbia	Vice-President, Wood Products, Northern B.C.
G.B. Hobson North Vancouver, British Columbia	Vice-President and Corporate Controller
W.B. Jacques(2) Grande Prairie, Alberta	Vice-President, Alberta Operations
B.F. King(3) Vancouver, British Columbia	Vice-President, Human Resources
A.K. MacMillan Delta, British Columbia	Vice-President, Environment
R.F. Weinman North Vancouver, British Columbia	Vice-President and Secretary
R.B. Haslam North Vancouver, British Columbia	Deputy Corporate Controller
J.K. Pau Vancouver, British Columbia	Treasurer

(1) *Mr. Bickell is retiring on March 1, 1992*
(2) *Mr. Jacques left Canfor on January 31, 1992*
(3) *Mr. King joined Canfor on January 7, 1992*

All of the above directors and officers have had the same or similar principal occupations with the organizations indicated for the last five years except that: prior to October 1987, Mr. Phelps held various executive positions with Westcoast Energy Inc.; prior to May 1989, Mr. Nielssen held various executive positions, most recently Executive Vice-President, with Canadian Pacific Forest Products Ltd. and with its predecessor companies CIP Inc. and The Tahsis Company Ltd.; prior to February 1992, Mr. King was Vice-President, Human Resources and Public Relations with Lasco Steel, a division of Co-Steel Inc.; and prior to June 1989, Mr. Stoilen held various executive positions with Canadian Airlines International Ltd., with its predecessor company, Canadian Pacific Airlines Limited and with its subsidiary, Eastern Provincial Airways, Inc.

Shareholdings of Directors and Senior Officers

As at January 31, 1992 the directors and senior officers of the Company, as a group, beneficially owned, directly or indirectly, or exercised control or direction over 432,900 Common Shares.

In addition, Matthews-Cartier Holdings Limited ("MCHL") owned 11,334,715 Common Shares representing approximately 43.8 per cent of the outstanding Common Shares of the Company. MCHL is owned indirectly by trusts for the benefit of members of the Prentice and Bentley families of Vancouver. The late Mr. J.G. Prentice and the late Mr. L.L.G. Bentley were the founders of Canfor. Mrs. M.E. Hurst and Mrs. E.R. Jarvis are the daughters of Mr. and Mrs. Prentice and Mr. P.J.G. Bentley is the son of Mr. and Mrs. Bentley. Under a Voting Agreement to which MCHL and the trustees of the trusts are parties, the Common Shares owned by MCHL will be voted for the election of one nominee of the Hurst family, one nominee of the Jarvis family and two nominees of the Bentley family. Mrs. M.E. Hurst, Mr. J.B. Jarvis, Mr. P.J.G. Bentley and Mrs. B.R. Hislop (daughter of Mr. and Mrs. P.J.G. Bentley) are the nominees and are directors of the Company and trustees of the trusts. Members of the families and their associates owned, in addition, approximately three per cent of the outstanding Common Shares.

Markets For Securities

The Common Shares are listed on the Toronto and Vancouver stock exchanges and the Class A Preferred Shares, Series 1 of the Company are listed on the Toronto stock exchange.

Dividends

The declaration and payment of dividends is at the discretion of Canfor's Board of Directors. The following dividends (per share) were paid in the years ended December 31 in 1991 and 1990.

	1991	1990
Class A Preferred Shares, Series 1	**$2.25**	$2.25
Common Shares	**0.45**	0.55

The amount of dividends the Company is permitted to pay under its term loan agreements is determined by reference to consolidated net earnings less certain restricted payments. As at December 31, 1991, the Company would be permitted under these agreements to pay up to $17 million or $0.65 per common share in dividends on its Common Shares. The agreements do not restrict payment of dividends on preferred shares.

Legal Proceedings

Proceedings were commenced on July 17, 1991 in the United States District Court for the District of Colorado against Canadian Forest Products Ltd. and 14 other Canadian forest products companies under U.S. antitrust legislation. The plaintiff, Rivendell Forest Products Ltd., a lumber wholesaler carrying on business in the United States, alleges that the defendants have engaged in a conspiracy in restraint of trade to artificially raise, fix, maintain or stabilize prices for Western Canadian softwood lumber sold to purchasers in the United States by charging the plaintiff and others artificially high freight prices. The plaintiff seeks to represent a class of all U.S. purchasers of Western Canadian softwood lumber products from the defendants during the period from August 1, 1987 to the date of the action. On behalf of this class, the plaintiff seeks damages in amounts which are presently undetermined but it is anticipated that the amounts will be substantial. Under the applicable law, the plaintiff may recover three times the amount of any damages awarded, plus costs and attorneys' fees. The defendants have filed motions to dismiss the complaint on jurisdictional grounds. The Canadian government has filed a brief urging the court to weigh the interests of Canada in deciding whether to exercise jurisdiction. Canadian Forest Products Ltd. denies the allegations and will defend against any proceedings under U.S. or Canadian law. Canfor strongly believes the allegations are without substance but because of the preliminary nature of the proceedings, no meaningful assessment of the likely outcome can be made by legal counsel.

Following the termination of the Memorandum of Understanding on Softwood Lumber ("M.O.U.") between the United States and Canada in October 1991, a bonding requirement has been established by United States Customs for imports of Canadian softwood lumber. In addition, the United States Department of Commerce announced the initiation of a countervailing duty investigation relating to softwood lumber products from Canada. At present, because of prevailing stumpage rates in British Columbia which were adopted after entry into the M.O.U. in 1987 as a replacement measure for the federal export tax, imports of lumber from British Columbia are subject to a zero-rated bond. This situation may change as a result of the outcome of the countervailing duty investigation.

Security

The Company's operating lines of credit and term indebtedness are unsecured.

Additional Information

Reference is made to the sections of this Annual Statutory report entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Financial Statements" which are incorporated by reference.

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of the Company's securities, options to purchase securities and interests of insiders in material transactions, where applicable, is contained in the information circular for the Annual General Meeting of the Company to be held on April 27, 1992. Copies of the information circular may be obtained upon request from the Secretary of the Company, 2800 - 1055 Dunsmuir Street, Vancouver, British Columbia V7X 1B5.

Canfor Corporation

Management's Discussion and Analysis of Financial Condition and Results of Operations

1991

Summary of Operating Results

	Year Ended December 31 1991	1990
	(millions of dollars)	
Segmented operating income (loss)		
Pulp and sack kraft paper	**$(11.0)**	$ 53.5
Wood and wood products	**(39.1)**	(27.9)
	(50.1)	25.6
Non-segmented expenses	**(47.6)**	(41.8)
Non-recurring items	**(3.2)**	39.0
Income (loss) of affiliated companies before tax	**(60.2)**	(8.2)
Income (loss) before income taxes	**(161.1)**	14.6
Income taxes (expense) recovery	**62.0**	(10.8)
Net income (loss) before extraordinary items	**$(99.1)**	$ 3.8
Extraordinary items	**5.2**	—
Net income (loss)	**$(93.9)**	$ 3.8
Cash flow from operations	**$(36.2)**	$ 94.9
	(dollars per common share)	
Net income (loss) — before extraordinary items	**$(4.18)**	$ 0.07
— after extraordinary items	**(3.96)**	0.07
Cash flow from operations	**(1.58)**	4.06

Operating Results

Canfor's net loss of $93.9 million after extraordinary items for 1991 was $97.7 million worse than the net income of $3.8 million for 1990. Extraordinary items reduced the 1991 net loss by $5.2 million from a total of $99.1 million. Canfor's operating loss (before non-segmented income and expenses and non-recurring items) was $50.1 million, an unfavourable change of $75.7 million from 1990.

For the second consecutive year poor market conditions for forest products, as evidenced by a one-third drop in pulp prices and low lumber prices, high stumpage rates that did not reflect those market conditions, and continued strengthening of the Canadian dollar relative to the United States dollar resulted in a severe decline in Canfor's results.

In the Pulp and Sack Kraft Paper segment, operating income decreased by $64.5 million from a $53.5 million income in 1990 to an $11.0 million operating loss in 1991. The primary cause of this unsatisfactory result was the decline, which started in the third quarter of 1990, of market pulp list prices from US$840 per tonne for the first two quarters of 1990 to US$720 per tonne in January 1991 and down to US$500 per tonne in October and November 1991. During 1990, as the result of increased pulp production capacity and the economic recession, papermakers chose to reduce the pulp inventories they had built up as protection in the preceding years of tight supply. During 1991, the continuance of the recession in North America and some other markets, coupled with pulp supply in excess of demand, gave papermakers no incentive to build inventories. Furthermore, while paper consumption worldwide increased by approximately 1.5 per cent in 1991 over 1990, the addition of new paper production capacity created an excess of paper supply over demand.

These factors not only resulted in the noted decline in list prices in 1991 but also created a situation in which actual transactions at prices below published list prices were quite common. The price decline appeared to end late in the year and Canfor announced a US$20 per tonne price increase in December 1991. A price increase to US$540 per tonne has been announced for February 1992 and a further increase of US$40 per tonne has been announced for April 1992. The impact of lower pulp prices on operating income is estimated at $60.5 million for 1991, compared to $9.5 million for 1990.

The other most significant factor which had an adverse effect upon operating income from the Pulp and Sack Kraft Paper segment in 1991 was the continuation of the increase in the value of the Canadian dollar relative to the United States dollar, in which currency the majority of Canfor's pulp and paper is sold. During 1991, the Canadian dollar changed from an average of $1.00 U.S. equal to $1.1688 Cdn. for 1990 to $1.00 U.S. equal to $1.1458 Cdn. for 1991. In 1991, this strengthening of the Canadian dollar had the effect of reducing operating income by an estimated $4.7 million.

Canfor's pulp and paper mills operated at 92 per cent of capacity during 1991 (82 per cent for 1990) as the result of 53 days (120 days for 1990) of curtailment of operations at the Prince George Pulp and Paper and Intercontinental Pulp mills to reduce inventories. Pulp production from these mills for 1991 was 362,000 tonnes and shipments were 372,000 tonnes, compared to 326,000 tonnes and 305,000 tonnes respectively in 1990. Included in the 1991 shipments were approximately 48,000 tonnes of pulp which received a premium price as the result of being bleached without the use of elemental chlorine in the bleaching process.

The market for kraft paper was adversely affected by the North American recession and general oversupply, with the result that prices decreased by approximately three per cent in 1991 from the 1990 level.

Pulp and paper manufacturing cost decreased by 8.7 per cent or approximately $50 per tonne in 1991 from 1990 levels. Approximately $35 per tonne of this decrease was attributable to lower wood chip prices since Canfor's wood chip purchase agreements in the interior of British Columbia tie the price paid for wood chips to the price received for pulp. To ease the impact on its chip suppliers, Canfor did not take full advantage of the drop in pulp prices on the chip pricing formula. Had it done so, pulp and paper manufacturing costs would have been reduced a further $18 per tonne. The remainder of the decrease in pulp and paper manufacturing cost is primarily the result of absorbing certain fixed costs over the greater aggregate production volume in 1991 than in 1990.

In the Wood and Wood Products segment, the loss from operations increased by $11.2 million to $39.1 million, from $27.9 million in 1990. The strengthening of the Canadian dollar relative to the United States dollar, in which currency the majority of Canfor's lumber is sold, caused approximately $5.0 million of this increased loss. In 1990, the strengthening of the Canadian dollar reduced operating income by an estimated $5.1 million. An increase of approximately $4.8 million in the amount of stumpage and royalties paid to the provinces of British Columbia and Alberta, from $50.6 million in 1990 to $55.4 million in 1991, was the other significant component of this unfavourable increase in the loss.

While new housing starts in North America continued to decline (from 1.58 million units in 1989 to 1.37 million units in 1990 and to 1.17 million units in 1991), Canfor was able to increase slightly its lumber sales volume by 2.4% in 1991 over 1990 (after giving effect to the sale of the High Level, Alberta mill on April 30, 1990). This was accomplished primarily as the result of Canfor's program to emphasize overseas markets and specialty products. This effort increased the shipments to overseas markets from six per cent of total sales in 1990 to 12 per cent in 1991.

Primarily as the result of a brief surge in lumber prices in the second quarter of 1991, caused by North American lumber dealers anticipating an economic recovery which did not materialize, Canfor's mill net return on lumber increased in 1991 by approximately three per cent (before the adverse impact of the U.S. - Canadian dollar exchange rate).

Non-segmented expenses, i.e., the net expenses, other than income tax, that are not directly related to the operation of the individual business segments, increased from $41.8 million in 1990 to $47.6 million in 1991. Of this $5.8 million increase, interest expense was responsible for $5.5 million, increasing from $19.8 million in 1990 to $25.3 million in 1991. In spite of lower interest rates in 1991, increased borrowings to fund the losses from operations and the capital expenditure program were responsible for this increase in interest expense. See "Summary of Financial Position".

Non-recurring items resulted in a $3.2 million loss in 1991 as compared to a $39.0 million income in 1990. In 1991, non-recurring items primarily consisted of a provision of $5.0 million for costs relating to the reduction of hardboard production and $1.8 million for a write-down of the fingerjoint plant at Grande Prairie, Alberta. These were partially offset by a $3.7 million business interruption insurance claim arising from the fire at the Fort St. James sawmill in January 1991. In 1990, non-recurring items related primarily to sales of assets. Note 18 to the Financial Statements describes the non-recurring items in detail for both years.

Canfor's equity in the loss of affiliated companies before tax increased by $52.0 million in 1991, to a loss of $60.2 million for 1991 compared to loss of $8.2 million for 1990. As detailed in the Schedule of Investments in Affiliated Companies, at Equity, in the Financial Statements, Howe Sound Pulp and Paper Limited ("Howe Sound") was responsible for $52.5 million of the increase in this loss. The drop in pulp prices and the strengthening of the Canadian dollar against the United States dollar, as discussed previously, were major factors contributing to the Howe Sound loss. Higher operating costs and lower than normal pulp production volumes relating to the start-up in late 1990 of the modernized and expanded pulp mill were also contributing factors on the pulp side. Also, additional costs were incurred in 1991 to produce the trial run of completely chlorine-free pulp for customers in the European market. Following completion of construction in April 1991, the newsprint mill, which was designed and constructed specifically to produce newsprint for the Japanese market, achieved a satisfactory start-up, although it did incur start-up costs. It is Canfor's policy to expense start-up costs as incurred rather than deferring them to be amortized as a charge against future years. During the period required to achieve the quality demanded by the Japanese market, much of the newsprint mill's production had to be sold in other markets in the face of low prices and oversupply in those markets. These were the main factors contributing $35.6 million of the $52.5 million increase in Canfor's share of Howe Sound's loss before income tax. Increased interest expense was responsible for the remaining $16.9 million. This increase in interest expense

primarily resulted from a combination of the elimination of interest income on cash and temporary investments as Howe Sound's funds were utilized in modernization and expansion of the pulp mill and the construction of the newsprint mill and the cessation of interest capitalization as the construction projects were completed.

Canfor's equity in the results of Canfor-Weldwood Distribution Ltd. ("CanWel") improved by $3.4 million in 1991 over the 1990 results. Thus, while CanWel's sales decreased by 18 per cent from 1990, the actions of management to control costs and inventory levels enabled CanWel to achieve a break-even position. Canfor's equity in the loss of B.C. Chemicals Ltd. and B.C. Chemicals Company increased by $2.8 million in 1991 over 1990, primarily as the result of interest expense on the loans provided to fund construction of the expanded sodium chlorate and tall oil facilities.

Canfor's net loss before income tax for 1991 was $161.1 million and, as described in detail in Note 14 to the Financial Statements, the income tax recovery of $62.0 million represents an effective tax recovery rate of 40.9 per cent, as compared to an effective income tax expense rate for 1990 of 59.4 per cent. This shift in effective tax rates is the result of the impact of Large Corporations Tax on the low level of taxable income in 1990 and the fact that during 1991 Howe Sound fully recovered prior years' deferred income taxes, with the result that a portion of the 1991 losses was not reduced by tax recoveries. At the end of 1991, Canfor's share of its affiliates' losses available to reduce their future income taxes amounted to $17.2 million.

In 1991, Canfor recorded an extraordinary gain of $5.2 million, after income taxes. The gain resulted because the property damage insurance proceeds realized in respect of the fire at the Fort St. James sawmill exceeded the net book value of the assets destroyed. There were no extraordinary items in 1990.

As discussed under the heading Changes in Financial Position below, cash flow from operations decreased by $131.1 million in 1991, from a net cash generated of $94.9 million in 1990 to net cash usage of $36.2 million in 1991.

Future Outlook

The short-term outlook for Canfor is more encouraging than it was one year ago. While both Canada and the United States are still trying to extricate themselves from the recession that has impaired their economies, there are presently many signs of improvement in the factors which affect the Canadian forest industry. The Canadian dollar has weakened significantly against the United States dollar. Interest rates are at the lowest levels in the past 19 years and, it appears, will remain at low levels for some time. In addition to reducing Canfor's interest costs, these lower rates should assist in stimulating construction and thus the demand for building products. Lumber prices have recently increased as factors such as withdrawals of timber lands and sawmill closures for economic and timber supply reasons take effect. Demand for Spruce/Pine/Fir ("SPF") lumber is increasing as its strength properties are becoming better recognized. Pulp prices appear to have bottomed at the end of 1991, and recently announced list price increases are expected to hold. Lumber distributors and papermakers appear willing to build inventories again rather than holding back in anticipation of possibly lower prices as they basically had been doing since the last half of 1990. If the improvements in market prices and demand presently indicated hold through 1992, Canfor's results will be significantly improved over 1991.

In 1991, Canfor had its lowest lost-time accident frequency in recent years. Canfor equates safety with a positive attitude and a commitment to excellence. Thus, management believes Canfor's people are ready and enthusiastically able to take advantage of the improving operating climate.

The sensitivity of Canfor's results to changes in the prices for its major products and in the value of the Canadian dollar relative to the United States dollar, expressed in terms of annual after-tax earnings (including its equity in the incomes of its affiliated companies), is as follows:

	(millions of dollars)
Lumber — $10 Cdn. change per mfbm	8.1
Pulp — $10 Cdn. change per tonne	3.5
Kraft paper — $10 Cdn. change per tonne	0.5
Newsprint — $10 Cdn. change per tonne	0.9
Canadian dollar — $0.01 U.S. change relative to $1.00 Cdn.	4.8

Early in 1992, Canfor completed a restructuring of management, which it commenced in late 1991. The restructuring involved realigning its operations into three business units: Coastal Operations, Northern Wood Products (essentially comprised of those operations manufacturing and marketing SPF wood products) and Pulp and Paper. Each of these units is headed by a Group Vice-President and each unit integrates marketing, production and raw material supply with the overall objective of better meeting customer needs. Canfor believes with this new structure and the new people added to complete it, that it is better positioned to aggressively compete on a world-wide scale in a market that is increasingly oriented to quality and customer service.

For the longer term, while there are many risks and uncertainties facing Canfor and the rest of the forest industry, as discussed in detail later under Risks and Uncertainties, Canfor believes the strength of its people, its willingness and demonstrated ability to address environmental concerns responsibly and the strategic actions taken over recent years to reduce debt, modernize its asset base, secure an appropriate fibre supply for its mills and tailor its products to meet the needs of its customers have positioned the company well to generate returns satisfactory to its shareholders on capital employed and shareholders' equity in periods of better economic conditions than those experienced in the past two years. Furthermore, Canfor believes its research and development efforts will provide the advantages of new or improved products and processes thus maintaining leadership in meeting and creating changes in the markets for forest products.

Summary of Financial Position

The following table summarizes Canfor's financial position as at the end of the years 1991 and 1990.

	1991	1990
	(millions of dollars)	
Net cash (net short-term indebtedness)	**$ (55.6)**	$ (10.4)
Operating working capital	**149.9**	152.5[1]
Current portion of long-term debt	**(4.3)**	(9.4)
Income taxes recoverable (payable)	**(2.3)**	2.8
Net working capital	**87.7**	135.5[1]
Long-term investments	**327.4**	308.6
Property, plant, equipment and timber	**593.6**	593.9
Other assets and deferred charges	**12.2**	10.4
Net assets	**$1,020.9**	$1,048.4
Long-term debt	**$ 267.5**	$ 221.0
Deferred reforestation	**21.1**	17.3[1]
Other long-term liabilities	**4.2**	3.6
Deferred income taxes	**87.6**	129.8
Deferred gain and deferred credit	**54.7**	60.1
Preferred share capital	**24.5**	25.0
Common shareholders' equity	**561.3**	591.6
Total capitalization	**$1,020.9**	$1,048.4
Ratio of current assets to current liabilities	**1.4:1**	1.8:1[1]
Ratio of total debt to shareholders' equity	**36:64**	28:72

(1) *These figures have been restated to conform with the 1991 presentation.*

Changes in Financial Position

Canfor's net working capital was reduced by $47.8 million during 1991 primarily as the losses and capital expenditures incurred in 1991 resulted in a $45.2 million increase in net short-term indebtedness.

Long-term investments increased by $18.8 million, reflecting investments or advances of $60 million in Howe Sound, $4.1 million to B.C. Chemicals Company and $1.0 million to CanWel during the year. These investments and advances, which were partially reduced by the $46.5 million equity in the losses of the affiliated companies during 1991, were required to offset the financial effects of the recession and, in the case of Howe Sound, the weakening of pulp markets and the start-up of new and expanded facilities and to meet construction costs not originally planned.

The carrying value of property, plant, equipment and timber remained virtually unchanged during 1991 as capital expenditures of $54.1 million were offset by depreciation and asset disposals. 1990 capital expenditures were $105.3 million.

Canfor increased its long-term debt by a net $41.4 million during 1991. Similar to the increase in net short-term indebtedness, these funds were applied to finance the losses and capital expenditures incurred in 1991. As at the end of 1991, the ratio of total debt to shareholders' equity increased to 36:64, compared to 28:72 at the end of 1990.

The long-term portion of Canfor's deferred reforestation liability increased by $3.8 million in 1991 to $21.1 million from $17.3 million at the end of 1990. This increase is essentially a reflection of the increasing cost of reforestation activities and an emphasis on quickly returning the harvested land to a reforested state.

Canfor's deferred income taxes liability decreased by $42.2 million in 1991 as the result of the losses incurred during the year.

Under the terms of its outstanding preferred shares, commencing in the third quarter of 1991 Canfor was required to make all reasonable efforts to purchase for cancellation, at a price not exceeding $25.00 per share plus costs of purchase, one per cent of the number of preferred shares outstanding at June 30, 1991. During the second half of 1991, 20,000 of the preferred shares were purchased, thus reducing the outstanding preferred shares by $500,000. The purchase of these shares below their par value of $25.00 resulted in a contributed surplus of $50,000.

Common shareholders' equity decreased by a net of $30.3 million during 1991. The major components of this change were the net loss of $93.9 million, plus $13.3 million in dividends paid to common and preferred shareholders. These components were partially offset by gross proceeds of $78.7 million from the issue of 3 million new common shares at a price of $26.125 per share and the exercise of stock options during the year. The effect was to reduce book value per common share from $25.90 per share at the end of 1990 to $21.70 per share at the end of 1991. During 1990, common shareholders' equity decreased by $10.4 million, from $26.38 per share at the end of 1989 to $25.90 per share at the end of 1990. This decrease was primarily the result of dividends on preferred and common shares of $14.8 million exceeding net income of $3.8 million.

Cash used in operating activities was $36.2 million in 1991 compared to $94.9 million of cash generated in 1990. This primarily resulted from a $72.0 million operating loss in 1991, down from an operating income of $4.4 million in 1990. This decrease in operating income is discussed in detail under "Operating Results". In 1990, cash generated from operating activities included $76.8 million proceeds on the sale of the operations at High Level, Alberta.

Operating working capital decreased by $2.6 million in 1991. There were no unusual components of this change. During 1990, operating working capital decreased by $6.4 million. Included in this change was $18.3 million of working capital realized on the sale of the High Level operations, $10.0 million of short-term advances to CanWel converted to long-term, $21.9 million increase in working capital components resulting from the economic slow-down in the second half of 1990 and a $21.2 million reduction of accounts payable and accrued liabilities as the result of repaying funds on loan to Canfor by certain directors, private companies controlled by such directors and individuals.

Interest payments increased by $5.5 million in 1991 over 1990 for the reasons discussed under "Operating Results". A net income tax recovery of $6.3 million was realized in 1991 as the result of recovering income tax instalments of approximately $8.3 million paid in 1990 prior to the commencement of losses caused by the economic downturn. This recovery was reduced by approximately $1.3 million of Large Corporations Tax paid in 1991 with the remainder being income taxes paid by subsidiary companies. In 1990, the taxes paid of $2.6 million were comprised of $1.6 million of Large Corporations Tax and $1.0 million of income taxes paid.

In 1991, Canfor's financing activities resulted in a cash inflow of $102.6 million compared to a cash outflow for 1990 of $29.8 million. During 1991, a net increase in long-term debt generated $40.9 million of cash and the issue of 3,024,190 common shares generated an additional net $75.3 million. Dividends to shareholders amounted to $13.3 million. During 1990, net repayments of long-term debt amounted to $15.3 million and dividends to shareholders amounted to $14.8 million.

Canfor's investing activities in 1991 required $111.6 million of cash as compared to $108.4 million in 1990. The major components of the 1991 cash requirements were $46.1 million for capital expenditures, net of $8.0 million of capital expenditures financed by insurance recoveries from the Fort St. James fire, and $65.1 million of investments in and advances to the affiliated companies, as described previously in this section. In 1990, capital expenditures amounted to $105.3 million and there were no investments in or advances to affiliates.

Financial Requirements and Liquidity

During 1991, Canfor improved its liquidity by drawing down US $40.0 million under a term debt facility established in 1990 and selling three million common shares, which raised $75.0 million after the costs of issue.

Canfor has planned capital expenditures of approximately $47 million for 1992. In addition, it has commitments of $4.3 million for debt repayment and $2.2 million for preferred share dividends. In February 1992, Canfor subscribed for an additional $15 million of preferred shares of Howe Sound to offset the financial effects of low pulp prices. Cash generation from operations is not expected to be sufficient to meet these requirements and, accordingly, Canfor expects to draw down on bank credit facilities during 1992 to fund its cash requirements. Canfor may refinance a portion of its bank indebtedness through an additional issue of debt or equity securities.

As at December 31, 1991, Canfor had current bank debt of $49.4 million and its ratio of current assets to current liabilities was 1.4:1. The Company has bank operating lines of credit of $195 million available. At the end of 1991, under the terms of its long-term borrowing agreements, Canfor had the capacity to incur additional long-term debt of approximately $235 million.

Approximately $16.5 million of Canfor's capital expenditures planned for 1992 are for the completion of projects commenced in 1991 or prior. Most notable of these are the modernization of the control systems at the Prince George Pulp and Paper mills and completion of environmental enhancement commitments. In 1991, Canfor commenced two major capital projects with an estimated total cost of approximately $110 million at its Intercontinental Pulp mill in Prince George which will further improve the mill's environmental performance and enable it to produce products meeting the higher environmental standards being demanded by some market sectors. Completion of these projects is presently planned for 1994, unless cash generated from operations improves sufficiently to justify earlier spending.

Over the past five years Canfor has expended $427 million on capital programs resulting in the modernization of its lumber mills, modernization of the instrument and control systems at its pulp and paper mills and the improvements necessary to meet or exceed present and some of the proposed new environmental regulations. While opportunities for additional capital expenditures offering attractive rates of return still exist, as the result of its recent capital spending Canfor can, if necessary to avoid increasing debt to levels it considers undesirable, maintain only a sustaining level of capital expenditures until the markets for its products improve sufficiently to fund greater capital spending.

Risks and Uncertainties

Virtually all companies in the forest industry in North America, including Canfor, face similar business risks and uncertainties. These risks and uncertainties fall into the general business areas of markets, currency, environmental issues, forest land base and, for Canadian companies, trade barriers.

Demand for forest products, both pulp and paper and wood products, are quite closely related to global business conditions and tend to be cyclical in nature, with product prices subject to volatile change. In 1989 the cycle for pulp and paper products peaked and it now appears the current cycle bottomed in late 1991. At present, the cycle appears to be turning toward higher prices and demand for Canfor's products, but some uncertainty and risk of reversal remains.

Canfor, like the rest of the Canadian forest products industry, competes in a truly international market. Thus, foreign currency relationships pose a significant uncertainty. Shifts in these relationships can have a significant impact, positive or negative, on profits from operations. By maintaining a substantial proportion of its debt in United States dollars, Canfor has partially mitigated the impact of currency fluctuations. The sensitivity of Canfor's results to currency swings and prices for its principal products is discussed under "Operating Results".

The forest industry in general is becoming increasingly subject to the pressures of a growing environmental awareness throughout the industrialized world. These pressures affect operations and the amounts of money that must be spent to meet new environmental regulations. Apart from having to comply with recent and proposed new federal and provincial regulations dealing with mill effluent, dioxins and furans, and organochlorines, the industry is currently facing the growing trend, coupled with legislated requirements, to recycle paper. In addition, the industry must be prepared to address new environmental initiatives raised by special interest groups.

In January 1992, for example, British Columbia's Minister of Environment, Land and Parks announced the intention of the provincial government to revise substantially its existing environmental legislation over the next few years. While this raises a significant element of uncertainty, Canfor is heartened by the Minister's statement, when making this announcement, in which he said "throughout the process, we want to work closely with the business community to ensure that the end result of all these new pieces of new legislation provides for a strong economic and environmental foundation for our province".

As discussed in more detail in Canfor's Annual Information Form under "Environment", Canfor has already met and exceeded recent legislative changes requiring reduction of AOX discharges and has virtually eliminated dioxins and furans in its effluent and pulp. Also, Canfor is well advanced in development of a pulp bleaching process which does not require the use of chlorine or chlorine compounds. This has already resulted in low AOX and chlorine-free pulp shipments being sold at premium prices. Canfor also believes that its long-fibred Northern Softwood Bleached Kraft pulp may experience increased demand and possibly higher prices because of demand for recycling. The long fibre pulp is required to add strength to paper manufactured from short, recycled fibre. Thus, while the environmental issues create uncertainty, they do not necessarily represent risks and do present opportunities to Canfor.

The Government of British Columbia is reviewing its forest tenure system and considering various proposals and recommendations to alter tenures and stumpage and royalty requirements. In addition, a new Commission on Resources and the Environment has been formed to develop and implement a land use plan for the province, with particular concern for the competing demands of the forestry industry, environmental protection and wilderness preservation groups, aboriginal land and self-government claims and other community interests. These initiatives raise uncertainties as to the future nature of forest tenure and the methods and extent of permitted logging operations. These uncertainties pose a risk for all companies in the forest products industry in British Columbia. However, any factor reducing the supply of timber available to the forest industry will eventually have the effect of increasing prices of forest products.

The countervailing duty investigation commenced by the United States Department of Commerce in respect of Canadian softwood lumber products poses some risk and uncertainty. Because of the prevailing level of stumpage rates in British Columbia, current exports of lumber from British Columbia to the United States are not significantly affected by the bonding requirements which have been imposed. However, depending upon the findings of the investigation, this situation may change and lumber prices may ultimately be affected.

The future effects of these uncertainties and potential risks cannot be quantified or predicted. However, Canfor does not foresee unmanageable adverse effects on its operations, and believes that it is well structured to deal with such matters as may arise and possibly to derive benefit from changes that may occur. In summary, Canfor's management believes that there are equally as many attractive opportunities for Canfor as there are risks and uncertainties, provided it continues to be innovative in its approach to these risks and uncertainties and responsive to the needs of its customers, and that it utilizes the strengths of its people and continues to operate in an environmentally responsible manner.

Canfor Corporation

Financial Statements

1991

Consolidated Statement of Income and Earnings Reinvested in the Business

(in Thousands of Dollars)	Year ended December 31 1991	1990
Net sales	**$822,479**	$884,350
Costs and expenses		
Manufacturing and product costs	**779,538**	767,449
Depreciation, depletion and amortization	**49,849**	43,977
Selling and administration	**65,132**	68,507
	894,519	879,933
Operating income (loss)	**(72,040)**	4,417
Losses of affiliated companies before tax	**(60,167)**	(8,158)
Interest expense *(Note 11)*	**(25,349)**	(19,834)
Other expenses	**(310)**	(798)
Non-recurring items *(Note 18)*	**(3,196)**	39,007
Income (loss) before income taxes	**(161,062)**	14,634
Income tax (expense) recovery *(Note 14)*		
Current	**(719)**	(4,466)
Deferred	**42,893**	(7,801)
Of affiliated companies	**19,835**	1,431
	62,009	(10,836)
Income (loss) before extraordinary items	**(99,053)**	3,798
Extraordinary items *(Note 17)*	**5,203**	—
Net income (loss)	**$(93,850)**	$ 3,798

Net income (loss) per common share (after provision for dividends on preferred shares)		
Before extraordinary items	**$ (4.18)**	$ 0.07
After extraordinary items	**$ (3.96)**	$ 0.07

Earnings reinvested in the business at beginning of year	**$348,660**	$359,668
Net income (loss) for the year	**(93,850)**	3,798
Preferred share dividends	**(2,235)**	(2,250)
Common share dividends	**(11,040)**	(12,556)
Contributed surplus *(Note 9)*	**50**	—
Share issue expenses, net of tax *(Note 9)*	**(1,960)**	—
Earnings reinvested in the business at end of year	**$239,625**	$348,660

Consolidated Cash Flow Statement

(in Thousands of Dollars)	Year ended December 31	
	1991	1990 *(Note 20)*
Cash generated from (used in)		
Operating activities		
Operating income	**$(72,040)**	$ 4,417
Depreciation, depletion and amortization	**49,849**	43,977
Proceeds on disposal of assets	**2,571**	79,871
Working capital changes	**(544)**	(3,633)
Other (including $3,415,000 of insurance proceeds in 1991)	**3,906**	(6,460)
	(16,258)	118,172
Interest — net of capitalized portion	**(26,200)**	(20,685)
Income tax	**6,303**	(2,557)
	(36,155)	94,930
Financing activities		
Long-term debt	**40,928**	(15,337)
Dividends paid to		
Preferred shareholders	**(2,235)**	(2,250)
Common shareholders	**(11,040)**	(12,556)
Net proceeds on issue of common shares *(Notes 9 and 10)*	**75,366**	337
Redemption of preferred shares *(Note 9)*	**(450)**	—
	102,569	(29,806)
Investing activities		
Property, plant, equipment and timber	**(54,060)**	(105,252)
Less: Financed by insurance recoveries *(Note 17)*	**7,991**	—
Investment in preferred shares of Howe Sound Pulp and Paper Limited	**(60,000)**	—
Advances to affiliates	**(5,150)**	—
Other	**(401)**	(3,099)
	(111,620)	(108,351)
Decrease in net cash	**(45,206)**	(43,227)
Net cash (net short-term indebtedness)* at beginning of year	**(10,382)**	32,845
Net short-term indebtedness at end of year	**$(55,588)**	$(10,382)
Operating working capital changes		
Accounts receivable	**$ (1,672)**	$ 38,980
Accounts receivable from affiliated companies	**112**	2,944
Inventories	**10,186**	(13,356)
Prepaid expenses	**(219)**	318
Accounts payable	**(24,640)**	(17,688)
Accounts payable to affiliated companies	**15,689**	(14,831)
	$ (544)	$ (3,633)

**Net cash (net short-term indebtedness) consists of cash, temporary investments, unpresented cheques and bank loans.*

Consolidated Balance Sheet

(in Thousands of Dollars)	December 31	
	1991	1990
ASSETS		
Current assets		
Cash and temporary investments	**$ 5,208**	$ 4,155
Accounts receivable		
Trade	**91,103**	93,486
Other	**17,997**	13,067
Affiliated companies	**930**	1,042
Income taxes recoverable	**—**	2,750
Inventories *(Note 2)*	**168,379**	178,630
Prepaid expenses	**2,501**	2,282
Total current assets	**286,118**	295,412
Long-term investments *(Note 3)*	**327,387**	308,638
Property, plant, equipment and timber *(Note 4)*	**593,590**	593,926
Deferred charges *(Note 5)*	**12,243**	10,473
	$1,219,338	$1,208,449

Auditors' Report

To the Shareholders of Canfor Corporation

We have audited the consolidated balance sheets of Canfor Corporation as at December 31, 1990 and December 31, 1991 and the consolidated statements of income and earnings reinvested in the business and cash flow for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 1990 and December 31, 1991 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles. As required by the British Columbia Company Act, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

Price Waterhouse

February 3, 1992
Chartered Accountants

	December 31	
	1991	1990 *(Note 20)*
LIABILITIES		
Current liabilities		
Unpresented cheques	**$ 11,382**	$ 9,629
Bank loans	**49,414**	4,908
Accounts payable and accrued liabilities	**106,719**	127,397
Accounts payable to affiliated companies	**24,257**	8,567
Current portion of long-term debt *(Note 6)*	**4,323**	9,409
Income taxes payable	**2,317**	—
Total current liabilities	**198,412**	159,910
Long-term liabilities		
Long-term debt *(Note 6)*	**267,513**	221,032
Deferred reforestation	**21,079**	17,318
Other liabilities	**4,250**	3,647
	292,842	241,997
Deferred income taxes	**87,588**	129,783
DEFERRED CREDIT *(Note 7)*	**2,855**	3,706
DEFERRED GAIN *(Note 8)*	**51,829**	56,436
SHAREHOLDERS' EQUITY		
Share capital *(Notes 9 and 10)*		
Preferred shares	**24,500**	25,000
Common shares	**322,150**	243,440
	346,650	268,440
Earnings reinvested in the business	**239,625**	348,660
Foreign exchange translation adjustment	**(463)**	(483)
	585,812	616,617
Commitments *(Note 13)*		
	$1,219,338	$1,208,449

APPROVED BY THE BOARD

Peter J.G. Bentley, Director

Ronald L. Cliff, Director

December 31, 1991

Basis of presentation of financial statements

These financial statements include the accounts of Canfor Corporation (the Company) and its subsidiary companies (Page 50), hereinafter referred to as "Canfor".

Canfor's investments in B.C. Chemicals Ltd., B.C. Chemical Company (an unincorporated joint venture), Heffley Reforestation Centre Ltd., Canfor-Weldwood Distribution Ltd., and Howe Sound Pulp and Paper Limited are accounted for on the equity basis.

Valuation of inventories

Inventories of wood products, pulp, sack kraft paper, logs and chips are valued at the lower of average cost and net realizable value. Processing materials and supplies are valued at the lower of average cost and replacement cost.

Property, plant, equipment and timber

Canfor capitalizes the costs of major replacements, extensions and improvements to plant and equipment, together with related interest expense incurred during the construction period on major projects.

The rates of depreciation are based upon depreciating the assets over the following estimated productive lives:

Buildings	10 to 40 years
Mobile equipment	3 to 20 years
Pulp and paper mill machinery and equipment	15 to 20 years
Sawmill machinery and equipment	4 to 12 years
Logging machinery and equipment	3 to 12 years
Logging roads and bridges	10 to 20 years
Other machinery and equipment	5 to 20 years

Depreciation of logging and manufacturing assets is calculated on a unit of production basis.

Depreciation of plant and equipment not employed in logging and manufacturing is calculated on a straight-line basis.

Amortization of logging roads is dependent upon their nature and is calculated on either a straight-line basis or on the basis of the volume of timber harvested.

Depletion of timber is calculated on the basis of the volume of timber harvested.

Deferred charges

Deferred financial costs are amortized over the lives of the related debt. Software development costs, relating to major systems, are deferred and amortized over periods not longer than ten years.

Pension costs

Canfor has various contributory and non-contributory pension plans which cover most salaried employees and certain hourly employees not covered by forest industry-union pension plans.

Earnings are charged with the cost of benefits earned by employees as services are rendered. Adjustments arising from pension plan amendments, experience gains and losses, and changes in assumptions are amortized to earnings over the estimated average remaining service lives of plan members.

The difference between amounts included in earnings and Canfor's contributions to the pension plan are included in deferred charges or accrued liabilities on the balance sheet.

Deferred reforestation

Canfor accrues the cost of the reforestation required under its timber harvest agreements at the time the timber is cut.

Deferred credit

Income is realized over the lives of the related debt.

Deferred gain

Income is realized over the estimated remaining life of the assets to which the gain is applicable.

Foreign currency translation

Foreign currencies are translated into Canadian dollars using the temporal method as follows:

> Monetary assets and liabilities at year-end or applicable hedged exchange rates; non-monetary assets and liabilities at historical rates; revenues and expenses at exchange rates prevailing at the time the transaction occurs.
>
> Exchange gains or losses are reflected in income immediately with the exception of unrealized translation gains or losses related to long-term monetary liabilities hedged by future revenue streams, which are deferred until realized.

Canfor's foreign operations are considered to be self-sustaining and the assets and liabilities are translated using the current rate method. The translation gain or loss is included as a component of shareholders' equity.

Income taxes

Canfor accounts for income taxes on the tax allocation method. Under this method, timing differences between reported and taxable income result in provisions for taxes not currently payable. Such timing differences arise principally as a result of claiming depreciation, depletion, amortization, deferred charges and pension expense for tax purposes at amounts differing from those charged to income.

Investment tax credits are accounted for using the cost reduction method.

1. Accounting policies

The principal accounting policies followed by Canfor are summarized under the caption "Summary of Principal Accounting Policies".

2. Inventories

	1991	1990
	($000's)	
Wood products, pulp and sack kraft paper	**$ 89,064**	$ 85,713
Logs and chips	**50,169**	62,644
Processing materials and supplies	**29,146**	30,273
	$168,379	$178,630

3. Long-term investments

Investments (50% interest) are accounted for on an equity basis (see Schedule of Investments in Affiliated Companies, Page 52).

	1991	1990
	($000's)	
Cost		
— common shares	**$266,283**	$266,283
— preferred shares	**60,000**	—
— long-term notes and advances	**15,150**	10,000
Equity in income (loss) since acquisition	**(20,033)**	26,462
	321,400	302,745
Deposits, loans and other investments at the lower of cost or written-down value	**5,987**	5,893
	$327,387	$308,638

4. Property, plant, equipment and timber

December 31, 1991	Cost	Accumulated depreciation and depletion ($000's)	Net book value
Land	**$ 9,928**	**$ —**	**$ 9,928**
Pulp and paper mills	**449,267**	**207,072**	**242,195**
Sawmills and hardboard mills	**374,958**	**200,353**	**174,605**
Logging buildings and equipment	**48,983**	**32,692**	**16,291**
Logging roads and bridges	**96,264**	**69,652**	**26,612**
Other equipment and facilities	**26,123**	**9,574**	**16,549**
Timber	**125,925**	**18,515**	**107,410**
	$1,131,448	**$537,858**	**$593,590**

Investment tax credits in the amount of $129,000 (1990 — $2,002,000) earned in the year have been credited to plant and equipment and are being amortized on the same basis as the related assets.

Included in the above are assets under construction in the amount of $3,832,447 (1990 — $26,191,407) which are not being depreciated.

December 31, 1990	Cost	Accumulated depreciation and depletion ($000's)	Net book value
Land	$ 9,984	$ —	$ 9,984
Pulp and paper mills	425,621	192,735	232,886
Sawmills, plywood and hardboard mills	365,458	186,965	178,493
Logging buildings and equipment	48,170	30,855	17,315
Logging roads and bridges	89,552	64,384	25,168
Other equipment and facilities	29,963	8,777	21,186
Timber	126,120	17,226	108,894
	$1,094,868	$500,942	$593,926

5. Deferred charges

	1991	1990
	($000's)	
Unrealized foreign exchange gain on long-term debt	**$ (2,561)**	$ (2,834)
Software development costs	**3,732**	4,096
Pension contributions in excess of expense	**10,510**	8,423
Debt issue and other expenses	**562**	788
	$ 12,243	$ 10,473

Amortization of deferred charges expensed during the year amounted to $983,000 (1990 — $868,000).

6. Long-term debt

	1991	1990
	($000's)	
The Prudential Insurance Company of America		
(a) $22,950,000 U.S. (1990 — $26,100,000 U.S.) note payable, interest at 8.875%, repayable in instalments in the years 1992-1998	**$ 26,624**	$ 30,302
(b) $50,000,000 U.S. note agreement, interest at 10.70%, repayable in 1994 *(Note 7)*	**58,005**	58,050
(c) $50,000,000 U.S. note agreement, interest at 10.625%, repayable in 1995 *(Note 7)*	**58,005**	58,050
(d) $50,000,000 U.S. note agreement, interest at 10.60%, repayable in 1996 *(Note 7)*	**58,005**	58,050
$60,000,000 U.S. term loan with a Canadian bank, repayable in instalments in the years 1994-1996, currently comprised of:		
(a) $40,000,000 U.S. term loan with floating interest rates ranging from LIBOR plus 0.375% to 0.625%, and	**46,404**	—
(b) $20,000,000 Cdn. (1990 — $25,000,000) term loan with interest rates ranging from 12.62% to 12.99%, convertible in 1992 to a $20,000,000 U.S. term loan with floating interest rates ranging from LIBOR plus 0.5% to 0.625%	**20,000**	25,000
Other loans	**2,762**	—
Capital leases	**2,031**	989
	271,836	230,441
Less: Current portion of long-term debt		
Bank and other loans	**108**	5,000
Notes and agreements payable	**3,654**	3,657
Amounts due on capital leases	**561**	752
	4,323	9,409
	$267,513	$221,032

The agreements relative to The Prudential Insurance Company of America contain provisions limiting the amount of indebtedness which the Company and designated subsidiaries can incur and the amount of dividends payable on its common shares. These provisions do not impair the Company's planned operations in the foreseeable future.

Repayments on long-term debt required in each of the next five years are as follows:

	($000's)
1992	$ 4,323
1993	$ 3,941
1994	$84,334
1995	$85,399
1996	$85,487

7. Deferred credit

	Original amount	Accumulated amortization ($000's)	Net book value
December 31, 1991	**$5,005**	**$2,150**	**$2,855**
December 31, 1990	$5,005	$1,299	$3,706

The deferred credit (premium) is the result of the sum of the proceeds received being in excess of the amounts of the long-term debt with The Prudential Insurance Company of America. This premium will be realized over the lives of the debt and thereby reduces the interest cost. *(Note 6)*

8. Deferred gain

	Original amount	Accumulated amortization ($000's)	Net book value
December 31, 1991	**$69,105**	**$17,276**	**$51,829**
December 31, 1990	$69,105	$12,669	$56,436

The deferred gain is the result of selling assets to Howe Sound Pulp and Paper Limited in 1988.

9. Share capital

Authorized

10,000,000 Class A non-voting preferred shares, with a par value of $25 each, of which
1,000,000 of such Class A preferred shares are designated $2.25 cumulative redeemable exchangeable Class A preferred shares, Series 1
2,000,000 of such Class A preferred shares are designated floating rate cumulative redeemable retractable Class A preferred shares, Series 2
50,000,000 common shares without par value

	1991	1990
	($000's)	
Issued		
980,000 Class A preferred shares, Series 1 (1990 — 1,000,000)	**$ 24,500**	$ 25,000
25,868,610 common shares (1990 — 22,844,420)	**322,150**	243,440
	$346,650	$268,440

On August 1, 1991 the Company issued for cash 3,000,000 common shares under a public offering at an issue price of $26.125 per share giving net proceeds of $75,030,000.

On April 30, 1990, the Company cancelled its 110,000 7% cumulative, redeemable non-voting preferred shares, with a par value of $100 each.

Class A preferred shares
The Class A preferred shares are entitled to preference over the common shares with respect to the payment of dividends.

Exchangeable Class A preferred shares
The exchangeable preferred shares entitled the holders at any time prior to the close of business on June 30, 1991 or the third business day prior to the date fixed for redemption, whichever was earlier, to acquire from Canfor .2778 Class A subordinate voting shares of B.C. Pacific Capital Corporation (formerly Versatile Corporation) which is equivalent to an exchange price of $90.00 per Class A subordinate voting share. On July 1, 1989, the exchangeable preferred shares became redeemable at $26.00 per share declining by $0.25 annually to $25.00 on and after July 1, 1993, in each case plus accrued and unpaid dividends.

During each calendar quarter and commencing in the first full calendar quarter following the expiry of the exchange privilege, the Company is required to make all reasonable efforts to purchase for cancellation, at a price not exceeding $25.00 per share plus costs of purchase, 1% of the number of exchangeable preferred shares outstanding on the expiry of the exchange privilege. This obligation is cumulative within each calendar year. During the second half of 1991, the Company purchased for cancellation 20,000 of these shares, resulting in a contributed surplus of $50,000.

The exchangeable preferred shares carry a right to cumulative preferred cash dividends at a rate of $2.25 per share per annum.

Common shares
The holders of the common shares have no pre-emptive, redemption or conversion rights.

10. Senior management stock option plan

The Company has established a Senior Management Stock Option Plan for officers and certain employees of Canfor. Under this plan, the Company has reserved for issue 700,000 common shares of which 158,105 will not be issued. Options of 48,760 common shares were outstanding at December 31, 1991 (1990 — 71,440). The exercise price for these options is between $13.75 and $24.375 per share with expiry dates until July 1994. In 1991, 24,190 common shares were issued under this plan (1990 — 26,585).

11. Interest expense

	Long-term	Short-term ($000's)	Total
December 31, 1991			
Total interest cost	**$24,259**	**$ 3,595**	**$27,854**
Less: Interest income	**348**	**865**	**1,213**
Interest capitalized	**—**	**1,292**	**1,292**
	$23,911	**$ 1,438**	**$25,349**
December 31, 1990			
Total interest cost	$24,933	$ 3,033	$27,966
Less: Interest income	118	7,062	7,180
Interest capitalized	—	952	952
	$24,815	$(4,981)	$19,834

12. Pension plans

Canfor has pension agreements which are unfunded under which certain present and former executive officers and directors of the Company are entitled to benefits. The present value of accumulated pension benefits based on projected service and compensation levels is $3,495,000 (1990 — $3,296,000).

Canfor's other pension plans have a present value of accumulated pension benefits based on projected service and compensation levels of $119,797,000 (1990 — $116,400,000). Plan net assets of $133,500,000 (1990 — $117,100,000) at market value are available for payment of these benefits.

Pension expense was $4,365,000 in 1991 after allowing for amortization of adjustments (1990 — $3,449,000).

13. Commitments

The future minimum lease payments under capital and operating leases are as follows:

	Capital leases ($000's)	Operating leases
1992	$ 746	$ 8,531
1993	429	7,772
1994	411	6,294
1995	372	5,339
1996	629	2,626
Thereafter	—	18,408
Total minimum lease payments	2,587	$ 48,970
Less amount representing imputed interest at rates ranging from 9.5% to 11.7%	556	
Present value of obligations under capital leases	2,031	
Due within one year	561	
Long-term obligations under capital leases	$ 1,470	

14. Income taxes

The computation of Canfor's income tax expense for 1991 and 1990 is as follows:

	1991 ($000's)	1990
Income (loss) before income taxes	**$(161,062)**	$ 14,634
Add (deduct)		
Items not deductible for tax purposes	**2,581**	12,390
Tax losses not recognized*	**10,307**	3,462
Portion of capital gains not subject to tax	**(2,636)**	(11,391)
Income not subject to tax	**(659)**	(852)
Accounting income (loss) for income tax purposes	**$(151,469)**	$ 18,243
Tax expense (recovery) at Canadian federal income tax rate of 38%	**$ (57,559)**	$ 6,932
Canadian manufacturing and processing allowance	**5,228**	(245)
Surtax on federal taxes	**(1,271)**	181
Provincial income taxes	**(7,566)**	682
Other tax adjustments	**(3,689)**	822
	(64,857)	8,372
Large Corporations Tax	**2,848**	2,524
Less applied to reduce surtax on federal taxes	**—**	(60)
Income tax expense (recovery)	**$ (62,009)**	$ 10,836
Effective tax (recovery) rate — excluding Large Corporations Tax	**(42.8)%**	45.6%
— including Large Corporations Tax	**(40.9)%**	59.4%

*Canfor's share of its affiliates' losses, $17,157,000 (1990 — $6,850,000) are available to reduce future income for tax purposes and expire in years ranging from 1996 to 1998.

15. Segmented information

Information relating to Canfor's business on a segmented basis is set out in the Statement of Segmented Information.

16. Related party transactions

Under agreements with Howe Sound Pulp and Paper Limited, Canfor supplies and obtains fibre at market prices, markets the pulp on a commission basis and provides certain management services.

During 1991, the Company subscribed for $60.0 million of redeemable preferred shares in Howe Sound Pulp and Paper Limited, and plans to subscribe for an additional $15.0 million in February 1992.

Under agreements with Canfor-Weldwood Distribution Ltd. Canfor sells lumber and hardboard at market prices, and rents warehouses previously used by its Building Materials Division at fair market value. During 1990, Canfor converted $5.0 million of long-term advances to Canfor-Weldwood Distribution Ltd. to share capital and converted $9.0 million of short-term advances to a long-term interest bearing promissory note on which the interest is currently being waived, and a further $1.0 million to a long-term non-interest bearing advance. A further $1.0 million was advanced during 1991 on a non-interest bearing basis.

During 1991, Canfor invested $4.15 million in B.C. Chemical Company.

17. Insurance claims

Canfor has submitted claims to the insurers in respect of a fire at the Fort St. James sawmill for business interruption, extra costs and property damage. The business interruption claim is for $3,698,000 and is reflected as a 'non-recurring' item in the income statement *(see Note 18)*. The property damage insurance proceeds exceeded the net book value of the fixed assets destroyed in the fire by $7,991,000. Consequently, Canfor has recorded an extraordinary gain in the amount of $5,203,000 net of income taxes.

18. Non-recurring items

	1991	1990
	($000's)	
Business interruption insurance claim *(Note 17)*	**$ 3,698**	$ —
Accrued costs of reduction in production of hardboard to a one press operation	**(5,000)**	—
Write-down of Grande Prairie fingerjoint plant	**(1,826)**	—
On April 30, 1990 the Company sold the assets of its High Level, Alberta operation		
Total consideration received		
Cash	—	78,042
Less expenses incurred on sale	—	1,258
	—	76,784
Net assets sold		
Working capital	—	18,104
Other assets	—	20,170
Liabilities assumed by purchaser	—	(3,768)
	—	34,506
Gain on sale	—	42,278
Cost of closure of Grande Prairie Plywood Division	**(393)**	(6,289)
Accrued costs of reduction of operation to one shift basis at Taylor Sawmill Division	—	(500)
Gain on disposal of property	**325**	3,518
	$ (3,196)	$ 39,007

19. Contingent liabilities

In July 1991, an antitrust suit was filed in Denver, Colorado alleging that Canadian Forest Products Ltd. and fourteen other Canadian companies raised prices on western Canadian softwood lumber sold to purchasers in the United States by charging artificially high freight prices. The management of the company believes that the case has no merit and the company intends to defend itself.

20. Comparative figures

Certain 1990 figures have been restated to conform with the 1991 presentation.

SUBSIDIARY COMPANIES *(Wholly-owned)*

Active

Balfour Guthrie Forest Products Inc.
Balfour Timber Limited
Canadian Forest Products Ltd.*
Canfor Europe (formerly Canadian Forest Products S.A.)
Canfor Hong Kong Corporation
Canfor Japan Corporation
Canfor U.S.A. Corporation
Howe Sound Transportation Company Limited

Inactive

Canadian Forest Products Overseas Limited (ceased trading operations on June 30, 1990)
Canfor Limited
Eburne Sawmills Limited

**Formed by an amalgamation of Canadian Forest Products Ltd., Balfour Forest Products Inc., Canfor Capital Limited and Canfor Investments Ltd. on January 1, 1990.*

Definitions of Selected Financial Terms

NET INCOME PER COMMON SHARE is the net income for the year, less provision for preferred dividends in the year, divided by the weighted average number of common shares outstanding during the year.

CASH FLOW FROM OPERATIONS PER COMMON SHARE is the cash flow from operations for the year, before interest and income tax, less provision for preferred dividends in the year, divided by the weighted average number of common shares outstanding during the year.

COMMON SHAREHOLDERS' EQUITY PER COMMON SHARE is the shareholders' equity excluding preferred share capital at the end of the year, divided by the number of common shares outstanding at the end of the year.

TOTAL CAPITALIZATION is comprised of long-term liabilities, deferred income taxes, deferred credit, deferred gain and shareholders' equity.

CAPITAL EMPLOYED consists of the funds invested or retained in the Company in the form of shares or liabilities. It is composed of unpresented cheques, current bank loans (net of cash and temporary investments), current portion of long-term debt, long-term debt, deferred income taxes, deferred credit, deferred gain and shareholders' equity. Long-term liabilities such as deferred reforestation costs and unfunded pension and retirement benefits are specifically excluded because they do not represent borrowed funds or funds invested by shareholders.

RETURN ON CAPITAL EMPLOYED is equal to net income plus interest, after tax, divided by the average of the capital employed as at the beginning and end of the year.

RETURN ON COMMON SHAREHOLDERS' EQUITY is equal to net income for the year, less provision for preferred dividends in the year, divided by the average of the shareholders' equity excluding preferred share capital at the beginning and end of the year.

NUMBERS OF EMPLOYEES AT YEAR-END is the actual number of employees, salaried and hourly, full-time and part-time, permanent and temporary, who are considered as employees of the Company. This number includes employees who are on vacation, leave of absence, workers' compensation, long-term disability or who are laid off as the result of temporary shut-down.

Statement of Segmented Information

Years ended December 31, 1991 and 1990

(in Millions of Dollars)

	Wood and Wood Products		Pulp and Paper		Consolidated	
	1991	1990	**1991**	1990	**1991**	1990
By Industry Segment						
Net sales						
To external customers	**$580.3**	$593.5	**$242.2**	$290.9	**$ 822.5**	$ 884.4
To other segments	**33.6**	42.7	—	—		
	$613.9	$636.2	**$242.2**	$290.9		
Segmented operating income (loss)	**$(39.1)**	$(27.9)	**$(11.0)**	$ 53.5	**$ (50.1)**	$ 25.6
Non-segment expenses					**(43.8)**	(21.8)
Net income (loss)					**$ (93.9)**	$ 3.8
Identifiable assets	**$425.4**	$444.9	**$352.1**	$348.0	**$ 777.5**	$ 792.9
Corporate assets and investments					**441.8**	415.5
Total assets					**$1,219.3**	$1,208.4
Depreciation, depletion and amortization	**$ 36.3**	$ 35.0	**$ 15.2**	$ 11.4		
Net capital expenditures	**$ 21.4**	$ 42.1	**$ 24.2**	$ 60.2		

1. *Sales to other segments are accounted for at prices which approximate market.*
2. *Operations are considered to be in one geographical area, since the operation of the subsidiary in the United States is not significant to the total. Export sales were $637 million in 1991 (1990 — $688 million).*
3. *The 1990 information for the Wood and Wood Products segment includes the High Level Division to the date of its sale, April 30, 1990 (Note 18).*

Schedule of Investments in Affiliated Companies, at Equity

(in Thousands of Dollars)

	Howe Sound Pulp and Paper Limited		Canfor-Weldwood Distribution Ltd.	
	December 31		December 31	
	1991	1990	**1991**	1990
Percentage Ownership	**50%**	50%	**50%**	50%
Investment				
Cost of investment	**$ 317,500**	$ 257,500	**$ 18,500**(C)	$ 17,500(C)
Equity in income (loss) since acquisition	**(13,496)**	29,483	**(6,716)**	(6,752)
Carrying value of investment	**$ 304,004**	$ 286,983	**$ 11,784**	$ 10,748
Equity Share of Results for the Year				
Net income (loss) of affiliated companies before tax	**$ (63,012)**	$ (10,504)	**$ 61**	$ (3,390)
Amortization of deferred gain	**6,328**	6,328	**—**	—
Total income (loss) of affiliated companies before tax	**(56,684)**	(4,176)	**61**	(3,390)
Income tax				
— affiliated companies	**20,035**	3,052	**(25)**	—
— amortization of deferred gain	**(1,721)**	(1,721)	**—**	—
Total income tax	**18,314**	1,331	**(25)**	—
Net income (loss) of affiliated companies	**(38,370)**	(2,845)	**36**	(3,390)
Less net amortization of deferred gain	**(4,607)**	(4,607)	**—**	—
Equity in net income (loss) of affiliated companies	**$ (42,977)**	$ (7,452)	**$ 36**	$ (3,390)
Summarized Financial Information of Affiliated Companies				
Assets	**$1,569,540**	$1,426,561	**$ 72,078**	$ 75,026
Liabilities	**961,532**	852,595	**48,510**	53,530
Shareholders' equity	**$ 608,008**	$ 573,966	**$ 23,568**	$ 21,496
Revenues of affiliated companies	**$ 169,361**	$ 117,070	**$415,922**	$508,910
Net income (loss) of affiliated companies	**$ (85,954)**	$ (14,904)	**$ 72**	$ (6,780)

Notes:

(A) *Canfor has entered into an agreement with B.C. Chemicals Ltd. and Northwood Pulp and Timber Ltd. to operate an unincorporated joint venture under the name of B.C. Chemicals Company. Canfor's equity interest directly and through its interest in B.C. Chemicals Ltd., is fifty percent. The joint venture is accounted for on the equity basis and the combined equity income of B.C. Chemicals Ltd. and B.C. Chemicals Company are shown here.*

(B) *For presentational purposes an income tax recovery of $1,555,000 arising on losses of the Joint Venture is included as part of affiliates taxes but excluded from the carrying value of the investment.*

(C) *Includes $9,000,000 (1990 — $9,000,000) note payable to Canfor on which interest is not currently being charged and $2,000,000 (1990 — $1,000,000) long-term advance on which interest is not currently being charged.*

(D) *Includes $4,150,000 advanced on a non-interest bearing basis during 1991.*

B.C. Chemicals Ltd. and B.C. Chemicals Company (A)		Heffley Reforestation Centre Ltd.		Total	
December 31		December 31		December 31	
1991	1990	**1991**	1990	**1991**	1990
50%	50%	**50%**	50%		
$ 4,650(D)	$ 500	**$ 783**	$ 783	**$ 341,433**	$ 276,283
481	3,791	**(302)**	(60)	**(20,033)**	26,462
$ 5,131	$ 4,291	**$ 481**	$ 723	**$ 321,400**	$ 302,745
$(3,301)	$ (520)	**$ (243)**	$ (72)	**$ (66,495)**	$ (14,486)
—	—	**—**	—	**6,328**	6,328
(3,301)	(520)	**(243)**	(72)	**(60,167)**	(8,158)
1,546(B)	100	**—**	—	**21,556**	3,152
—	—	**—**	—	**(1,721)**	(1,721)
1,546	100	**—**	—	**19,835**	1,431
(1,755)	(420)	**(243)**	(72)	**(40,332)**	(6,727)
—	—	**—**	—	**(4,607)**	(4,607)
$(1,755)	$ (420)	**$ (243)**	$ (72)	**$ (44,939)**	$ (11,334)
$74,730	$71,317	**$2,093**	$2,859	**$1,718,441**	$1,575,763
64,468	62,735	**1,131**	1,413	**1,075,641**	970,273
$10,262	$ 8,582	**$ 962**	$1,446	**$ 642,800**	$ 605,490
$24,092	$11,992	**$1,187**	$1,289	**$ 610,562**	$ 639,261
$(3,510)	$ (840)	**$ (485)**	$ (144)	**$ (89,877)**	$ (22,668)

Canfor Corporation
Ten Year Comparative Review

	1991	1990	1989	1988	1987	1986	1985	1984	1983	1982
Sales and income *(in millions of dollars)*										
Net sales	**$ 822.5**	$ 884.4	$ 921.2	$1,084.2	$1,244.9	$1,046.8	$1,083.8	$1,029.5	$ 995.1	$ 729.6
Manufacturing and product costs	**779.5**	767.5	686.1	824.3	915.8	847.7	997.1	908.4	881.3	700.5
Depreciation, depletion and amortization	**49.9**	44.0	41.3	38.0	43.4	37.7	45.3	45.1	48.6	45.0
Selling and administration	**65.1**	68.5	65.0	71.7	66.2	65.2	65.0	62.7	62.7	66.8
(Income) loss of affiliated companies before tax (a)	**60.2**	8.2	(37.4)	(35.4)	(0.5)	—	—	—	—	—
Interest expense	**25.4**	19.8	12.0	2.2	13.1	27.5	39.2	44.2	49.0	50.4
Other (income) expense	**0.3**	0.8	(1.9)	9.0	2.6	(11.3)	(29.5)	(2.9)	(0.4)	0.8
Non-recurring items	**3.2**	(39.0)	(7.6)	—	—	—	—	—	—	—
Income (loss) before income taxes	**(161.1)**	14.6	163.7	174.4	204.3	80.0	(33.3)	(28.0)	(46.1)	(133.9)
Income tax (expense) recovery	**62.0**	(10.8)	(67.3)	(72.8)	(98.3)	(52.8)	(20.7)	3.1	9.9	46.0
Income (loss) before undernoted items	**(99.1)**	3.8	96.4	101.6	106.0	27.2	(54.0)	(24.9)	(36.2)	(87.9)
Equity in income (loss) of affiliated companies (b)	**—**	—	—	—	—	—	(8.2)	1.4	(9.3)	(2.5)
Minority interests in subsidiaries	**—**	—	—	—	—	(1.2)	(0.3)	2.3	1.0	5.9
Income (loss) before extraordinary items	**(99.1)**	3.8	96.4	101.6	106.0	26.0	(62.5)	(21.2)	(44.5)	(84.5)
Extraordinary items and write-down	**5.2**	—	—	78.4	(3.3)	(2.3)	1.1	(2.6)	0.3	—
Net income (loss)	**(93.9)**	3.8	96.4	180.0	102.7	23.7	(61.4)	(23.8)	(44.2)	(84.5)
Preferred share dividends	**(2.2)**	(2.3)	(5.7)	(6.0)	(6.2)	(6.7)	(6.7)	(3.3)	(0.9)	(0.9)
Net income (loss) for common shareholders	**$ (96.1)**	$ 1.5	$ 90.7	$ 174.0	$ 96.5	$ 17.0	$ (68.1)	$ (27.1)	$ (45.1)	$ (85.4)
Per common share *(in dollars)*										
Before extraordinary items and write-down	**$ (4.18)**	$ 0.07	$ 3.98	$ 4.21	$ 4.41	$ 0.92	$ (3.73)	$ (1.31)	$ (3.09)	—
After extraordinary items and write-down	**(3.96)**	0.07	3.98	7.67	4.26	0.81	(3.67)	(1.45)	(3.07)	—
Dividends paid on common shares	**0.45**	0.55	0.70	0.55	0.35	—	—	—	—	—
Assets and capitalization *(in millions of dollars)*										
Working capital	**$ 87.7**	$ 135.5	$ 193.1	$ 129.1	$ 189.7	$ 61.7	$ 1.3	$ 48.5	$ 26.1	$ (118.6)
Long-term investments	**327.4**	308.6	307.7	387.1	62.3	66.0	22.5	73.1	73.9	84.9
Plant and equipment	**593.6**	593.9	569.0	363.9	430.5	420.8	454.6	448.7	451.6	479.5
Other assets and deferred charges	**12.2**	10.5	8.7	5.6	17.2	38.9	41.1	30.8	18.6	20.4
Net assets	**$1,020.9**	$1,048.5	$1,078.5	$ 885.7	$ 699.7	$ 587.4	$ 519.5	$ 601.1	$ 570.2	$ 466.2
Long-term liabilities	**$ 292.8**	$ 242.0	$ 263.5	$ 115.3	$ 149.1	$ 186.2	$ 198.8	$ 231.0	$ 242.3	$ 223.6
Deferred income taxes	**87.6**	129.8	122.4	103.3	110.3	41.8	20.5	0.6	1.6	15.5
Minority interests in subsidiaries	**—**	—	—	—	—	0.2	8.2	9.8	12.1	16.8
Deferred gain and credit	**54.7**	60.1	65.6	65.6	—	—	—	—	—	—
Preferred share capital	**24.5**	25.0	25.0	75.0	75.0	86.0	86.0	86.0	11.0	18.5
Common shareholders' equity	**561.3**	591.6	602.0	526.5	365.3	273.2	206.0	273.7	303.2	191.8
Total capitalization	**$1,020.9**	$1,048.5	$1,078.5	$ 885.7	$ 699.7	$ 587.4	$ 519.5	$ 601.1	$ 570.2	$ 466.2
Additions to property, plant and equipment *(in millions of dollars)*	**$ 54.1**	$ 105.3	$ 102.6	$ 107.8	$ 57.9	$ 37.9	$ 63.6	$ 41.0	$ 22.6	$ 102.4

Notes (a) *Income from affiliated forest industry companies in which 50% interest is held by Canfor.*
(b) *Equity income from affiliated non-forest industry companies in which less than 50% interest is held by Canfor.*

	1991	1990	1989	1988	1987	1986	1985	1984	1983	1982
Cash generated from (used in)										
(in millions of dollars)										
Operating activities	**$ (36.2)**	$ 94.9	$ 81.2	$ 180.7	$ 212.6	$ 126.9	$ 0.9	$ 28.8	$ (33.7)	$ (49.0)
Financing activities										
Long-term debt	**41.0**	(15.3)	70.4	(31.3)	(14.4)	(7.8)	(43.2)	(14.2)	17.8	65.2
Common and preferred shares	**75.4**	0.3	1.0	0.8	3.5	56.8	—	72.5	145.6	7.6
Dividends paid	**(13.3)**	(14.8)	(22.7)	(18.3)	(14.1)	(6.7)	(6.7)	(3.3)	(1.2)	(1.4)
Redemption of preferred shares	**(0.5)**	—	(50.0)	—	(11.0)	—	—	—	—	—
Realization of collateral account	—	—	55.0	—	—	(55.0)	—	—	—	—
	102.6	(29.8)	53.7	(48.8)	(36.0)	(12.7)	(49.9)	55.0	162.2	71.4
Investing activities										
Property, plant, equipment and timber	**(46.1)**	(105.3)	(102.6)	(107.8)	(57.9)	(37.9)	(63.6)	(41.0)	(22.6)	(102.4)
Dividends received	—	—	—	—	—	—	—	1.1	1.5	3.2
Investment in preferred shares of Howe Sound Pulp and Paper Limited	**(60.0)**	—	50.0	—	—	—	—	—	—	—
Extraordinary items	—	—	—	1.0	—	14.3	50.7	(2.6)	—	—
Investment in subsidiaries	**(5.1)**	—	(93.7)	—	—	—	—	—	—	—
Other	**(0.4)**	(3.0)	(8.0)	0.1	(0.4)	21.5	8.4	0.4	(1.4)	(3.2)
	(111.6)	(108.3)	(154.3)	(106.7)	(58.3)	(2.1)	(4.5)	(42.1)	(22.5)	(102.4)
Increase in net cash (net short-term indebtedness)	**$ (45.2)**	$ (43.2)	$ (19.4)	$ 25.2	$ 118.3	$ 112.1	$ (53.5)	$ 41.7	$ 106.0	$ (80.0)
Financial statistics										
Return on capital employed	**(7.6)%**	1.5%	11.2%	24.2%	16.3%	5.5%	(5.5)%	(0.1)%	(2.5)%	(7.8)%
Return on common shareholders' equity	**(16.7)%**	0.3%	16.0%	39.0%	30.2%	7.1%	(28.5)%	(9.3)%	(18.2)%	(36.4)%
Ratio of current assets to current liabilities	**1.4:1**	1.8:1	2.0:1	1.5:1	1.9:1	1.3:1	1.0:1	1.2:1	1.1:1	0.7:1
Ratio of total debt to shareholders' equity	**36:64**	28:72	30:70	19:81	30:70	43:57	60:40	52:48	58:42	71:29
Production statistics										
Pulp — *thousands of metric tons*	**362.7**	326.2	397.9	454.9	631.0	515.8	509.8	456.8	493.2	441.5
Sack kraft paper — *thousands of metric tons*	**90.8**	90.7	93.9	100.5	103.6	101.1	89.7	80.0	85.0	88.5
Lumber — *millions of board feet*	**1,354.8**	1,431.0	1,362.4	1,051.6	1,203.9	989.6	1,308.7	1,223.3	1,164.6	768.2
Plywood — *millions of square feet ⅜ inch equivalent*	**3.0**	63.9	68.7	68.1	69.4	109.2	281.0	293.3	298.3	223.0
Hardboard — *millions of square feet ⅜ inch equivalent*	**33.9**	35.8	36.2	35.4	36.4	35.2	55.9	56.9	57.5	43.0
Shingles and shakes — *thousands of squares*	—	—	—	—	111.6	108.6	117.4	102.9	127.3	144.1
Sales by product line										
Pulp and sack kraft paper	**29%**	33%	38%	38%	39%	30%	24%	25%	24%	33%
Lumber	**44**	41	43	25	26	23	27	26	28	19
Plywood and hardboard	**2**	3	3	3	2	4	7	7	8	8
Building materials purchased for resale	**22**	20	13	32	31	41	39	39	38	38
Miscellaneous	**3**	3	3	2	2	2	3	3	2	2
	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Sales by market										
Canada	**17%**	16%	17%	38%	32%	33%	37%	35%	35%	37%
United States	**41**	44	39	29	33	39	41	40	43	34
Europe	**25**	28	29	20	18	15	11	13	12	19
Far East	**16**	11	14	11	13	9	9	8	7	8
Other	**1**	1	1	2	4	4	2	4	3	2
	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Directors and Officers

Directors

A.G. Armstrong, Q.C.
Senior Vice-President, Finance, Canfor

P.J.G. Bentley, O.C.
Chairman and Chief Executive Officer, Canfor

R.L. Cliff, C.M.
Chairman of the Board, BC Gas Inc

C.W. Daniel, O.C.
Corporate Director/Consultant

M.H. Gunther
Vice-Chairman, Canfor

B.R. Hislop
Vice-President, Corporate Services,
Canadian Forest Products Ltd.

M.E. Hurst
Educational Author

J.B. Jarvis
Corporate Director

P.A. Lusztig
Former Dean, now Professor, Faculty of Commerce
and Business Administration,
University of British Columbia

A.S. Nielssen
President and Chief Operating Officer, Canfor

M.E.J. Phelps
President and Chief Executive Officer,
Westcoast Energy Inc.

R.T. Riley
Chairman of the Board,
Chateau Insurance Management Inc.

Officers

P.J.G. Bentley, O.C.
Chairman and Chief Executive Officer

M.H. Gunther
Vice-Chairman

A.S. Nielssen
President and Chief Operating Officer

A.G. Armstrong, Q.C.
Senior Vice-President, Finance

C.A. Arnesen
Group Vice-President, Pulp and Paper

P.J. Ashby
Group Vice-President, Northern Wood Products

S.T. Stoilen
Group Vice-President, Coastal Operations

G.B. Hobson
Vice-President and Corporate Controller

B.F. King
Vice-President, Human Resources

A.K. MacMillan
Vice-President, Environment

R.F. Weinman
Vice-President and Secretary

R.B. Haslam
Deputy Corporate Controller

J.K. Pau
Treasurer

Facilities

Principal Manufacturing Facilities and Annual Capacities

PULP, PAPER AND NEWSPRINT	Thousand tonnes
Prince George Pulp and Paper Division	
Prince George, B.C.	
Kraft pulp	170
Sack kraft paper	100
Intercontinental Pulp Division	
Prince George, B.C.	
Kraft pulp	235
Howe Sound Pulp and Paper Limited[A]	
Howe Sound Pulp and Paper Division	
Port Mellon, B.C.	
Kraft pulp	330
Newsprint	200
	1,035

LUMBER	Million board feet
Eburne Saw Mills Division	
Vancouver, B.C.	110
Northern Wood Products Operations:	
Bear Lake, B.C.	55
Chetwynd, B.C.	155
Fort St. James, B.C.	225
Fort St. John, B.C.	145
Isle Pierre, B.C.	95
Prince George, B.C.:	
Netherlands Division	230
Clear Lake Division	110
Taylor, B.C.	85
Grande Prairie, Alberta	155
Hines Creek, Alberta	70
Howe Sound Pulp and Paper Limited[A]	
Westcoast Cellufibre Division	
Vancouver, B.C.	40
	1,475

[A] *Howe Sound Pulp and Paper Limited is a 50 per cent owned affiliate of the Company.*

HARDBOARD	Million square feet ⅜ inch equivalent
Panel and Fibre Division	
New Westminster, B.C.	25

WOOD FIBRE PRODUCTS	Thousand tonnes
Panel and Fibre Division	
New Westminster, B.C.	
Baled wood fibre and fibre mat	25

SECONDARY MANUFACTURING

Canfor's United States subsidiary, Canfor U.S.A. Corporation, operates lumber remanufacturing facilities having a combined annual capacity of 135 million board feet in Meridian, Idaho and Bellingham, Washington. Canfor also produces remanufactured lumber products at a variety of its mill locations in British Columbia.

CHEMICALS MANUFACTURING

Two of Canfor's 50 per cent owned affiliates, B.C. Chemicals Ltd. and B.C. Chemicals Company, manufacture sodium chlorate for the pulp bleaching process and crude tall oil from a by-product of the pulping process.

NOTE:

Pulp, sack kraft paper, newsprint, hardboard and fibre product capacities are based on continuous operation for 344 days per year. The figure for Howe Sound's newsprint mill, which started up in mid-1991, is the design capacity. Capacities for lumber assume 240 operating days per year and two shifts per day, except for the Bear Lake and Taylor mills which are currently operating on a curtailed basis. All capacities are rounded figures and may differ from previously published values because of changes in mill facilities, log supply or product mix.

Sales and Distribution Facilities

PULP AND PAPER MARKETING OFFICES

Vancouver, B.C.
Brussels, Belgium
Tokyo, Japan

In addition, Canfor is represented by pulp and paper sales agents serving other markets around the world. The newsprint produced by Howe Sound Pulp and Paper Limited is marketed by Oji Paper Co., Ltd.

WOOD PRODUCTS MARKETING OFFICE

Vancouver, B.C.

WATERBORNE WOOD PRODUCTS SALES

Sales of Canfor's lumber to markets reached by ship are made exclusively through Balfour Guthrie Forest Products Inc., a wholly-owned subsidiary of Canfor, with offices in Vancouver, B.C. and the United Kingdom. Balfour Guthrie also markets wood products from a number of independent producers to a wide variety of overseas countries. Canfor's hardboard products are sold offshore by Seaboard Lumber Sales Company Limited and by the Panel and Fibre Division.

WHOLESALE BUILDING MATERIALS DISTRIBUTION

A 50 per cent owned affiliate of Canfor, Canfor-Weldwood Distribution Ltd., operates wholesale building materials distribution facilities in all major market areas across Canada.

Research and Development

Canfor operates a research and development facility in Vancouver, B.C. to conduct research relating to wood, fibre and pulp and paper manufacturing.

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